1968

CANADA

LAW REPORTS

RAPPORTS JUDICIAIRES

DU CANADA

Exchequer Court of Canada

Cour de l'Échiquier du Canada

PAUL A. RAYMOND, C.R.

M. I. PIERCE, B.A., LL.B.

Official Law Editors

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JUDGES

OF THE

EXCHEQUER COURT OF CANADA

During the period of these Reports:

PRESIDENT:

THE HONOURABLE WILBUR ROY JACKETT
(*Appointed May 4, 1964*)

PUISNE JUDGES:

THE HONOURABLE JOHN DOHERTY KEARNEY
(*Appointed November 1, 1951*)

THE HONOURABLE JACQUES DUMOULIN
(*Appointed December 1, 1955*)

THE HONOURABLE ARTHUR LOUIS THURLOW
(*Appointed August 29, 1956*)

THE HONOURABLE CAMILIEN NOËL
(*Appointed March 12, 1962*)

THE HONOURABLE ANGUS ALEXANDER CATTANACH
(*Appointed March 27, 1962*)

THE HONOURABLE HUGH FRANCIS GIBSON
(*Appointed May 4, 1964*)

THE HONOURABLE ALLISON ARTHUR MARIOTTI WALSH
(*Appointed July 1, 1964*)

THE HONOURABLE RODERICK KERR
(*Appointed November 1, 1967*)

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His Honour VINCENT JOSEPH POTTIER, Nova Scotia Admiralty District—appointed February 8, 1950.

The Honourable ARTHUR IVES SMITH, Quebec Admiralty District—appointed June 16, 1950.

The Honourable ROBERT STAFFORD FURLONG, Newfoundland Admiralty District—appointed October 8, 1959.

The Honourable DALTON COURTWRIGHT WELLS, Ontario Admiralty District—appointed January 28, 1960.

The Honourable THOMAS GRANTHAM NORRIS, British Columbia Admiralty District—appointed September 28, 1961.

The Honourable GEORGE ERIC TRITSCHLER, Manitoba Admiralty District—appointed October 19, 1962.

GORDON R. HOLMES, Q.C., Prince Edward Island Admiralty District—appointed May 24, 1963.

The Honourable HAROLD GEORGE PUDDESTER, Newfoundland Admiralty District—appointed June 4, 1963.

The Honourable JAMES DOUGLAS HIGGINS, Newfoundland Admiralty District—appointed May 28, 1964.

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His Honour REGINALD D. KEIRSTEAD, New Brunswick Admiralty District—appointed February 28, 1957.

The Honourable YVES BERNIER, Quebec Admiralty District—appointed November 17, 1965.

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ATTORNEY-GENERAL OF CANADA:

The Honourable JOHN TURNER

SOLICITOR GENERAL OF CANADA:

The Honourable G. J. MCILRAITH

JUGES

DE LA

COUR DE L'ÉCHIQUIER DU CANADA

en fonction au cours de la période de publication de ces rapports:

PRÉSIDENT:

L'HONORABLE WILBUR ROY JACKETT

(*nommé le 4 mai 1964*)

JUGES PUÎNÉS:

L'HONORABLE JOHN DOHERTY KEARNEY

(*nommé le 1er novembre 1951*)

L'HONORABLE JACQUES DUMOULIN

(*nommé le 1er décembre 1955*)

L'HONORABLE ARTHUR LOUIS THURLOW

(*nommé le 29 août 1956*)

L'HONORABLE CAMILIEN NOËL

(*nommé le 12 mars 1962*)

L'HONORABLE ANGUS ALEXANDER CATTANACH

(*nommé le 27 mars 1962*)

L'HONORABLE HUGH FRANCIS GIBSON

(*nommé le 4 mai 1964*)

L'HONORABLE ALLISON ARTHUR MARIOTTI WALSH

(*nommé le 1er juillet 1964*)

L'HONORABLE RODERICK KERR

(*nommé le 1er novembre 1967*)

JUGES DE DISTRICT EN AMIRAUTÉ DE LA COUR DE L'ÉCHIQUIER DU CANADA

L'honorable W. ARTHUR I. ANGLIN, district d'amirauté du Nouveau-Brunswick—nommé le 9 juin 1945.

Son honneur VINCENT JOSEPH POTTIER, district d'amirauté de la Nouvelle-Écosse—nommé le 8 février 1950.

L'honorable ARTHUR IVES SMITH, district d'amirauté de Québec—nommé le 16 juin 1950.

L'honorable ROBERT STAFFORD FURLONG, district d'amirauté de Terre-Neuve—nommé le 8 octobre 1959.

L'honorable DALTON COURTWRIGHT WELLS, district d'amirauté d'Ontario—nommé le 28 janvier 1960.

L'honorable THOMAS GRANTHAM NORRIS, district d'amirauté de la Colombie-Britannique—nommé le 28 septembre 1961.

L'honorable GEORGE ERIC TRITSCHLER, district d'amirauté du Manitoba—nommé le 19 octobre 1962.

GORDON R. HOLMES, C.R., district d'amirauté de l'Île du Prince-Édouard—nommé le 24 mai 1963.

L'honorable HAROLD GEORGE PUDDESTER, district d'amirauté de Terre-Neuve—nommé le 4 juin 1963.

L'honorable JAMES DOUGLAS HIGGINS, district d'amirauté de Terre-Neuve—nommé le 28 mai 1964.

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Son honneur REGINALD D. KEIRSTEAD, district d'amirauté du Nouveau-Brunswick—nommé le 28 février 1957.

L'honorable YVES BERNIER, district d'amirauté de Québec—nommé le 17 novembre 1965.

L'honorable ANDRÉ DEMERS, district d'amirauté de Québec—nommé le 26 novembre 1965.

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PROCUREUR GÉNÉRAL DU CANADA:

L'honorable JOHN TURNER

SOLLICITEUR GÉNÉRAL DU CANADA:

L'honorable G. J. MCILRAITH

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EN SA JURIDICTION DE COUR
DE PREMIÈRE INSTANCE

ET

EN SA JURIDICTION D'APPEL

BETWEEN:

SENSIBAR DREDGING CORPORATION LTD. .... APPELLANT;

Toronto 1967 Apr. 4-7, 17-18

Ottawa July 18

AND

THE MINISTER OF NATIONAL REVENUE .... RESPONDENT.

AND

BETWEEN:

CONSTRUCTION AGGREGATES CORPORATION .... APPELLANT;

AND

THE MINISTER OF NATIONAL REVENUE .... RESPONDENT.

Income tax—Company engaged in dredging business—Purchase of dredge on completion of contract—Transfer to subsidiary—Sale of dredge—Whether profit income or capital gain—Intention—Whether profit attributable to parent or subsidiary.

A company which carried on a world-wide dredging business operated five dredges in Canada for mining companies under contracts which gave it the right to buy them on completion of the contracts. With a view to expanding its Canadian operations it arranged to buy one of the dredges on completion of its contract, and while looking for work for the dredge was approached by a prospective purchaser of the dredge The company indicated interest in the proposition but nothing came of it and the company then obtained a dredging contract, purchased the dredge for $725,000, arranged to have it dismantled and reassembled in a different place at a cost of $340,000, and transferred its title to a subsidiary incorporated for that purpose. New proposals were then made by the prospective purchaser and after lengthy discussions the dredge and dredging contract were sold for $2,000,000

Held, the profit on the sale of the dredge should on the evidence be regarded as a profit of the subsidiary company rather than of the parent company; but whether made by either company the profit was a business profit and not a capital gain.

The parent company's intention in acquiring the dredge was not to use it as a dredge exclusively but to turn it to account by using it or disposing of it in any profitable way. Moreover the considerations which caused it to sell the dredge were related to its trading rather than its capital structure. Finally, the negotiations leading to sale of the dredge were characteristic of trading rather than mere realization of a capital asset.

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The subsidiary's intention in acquiring the dredge was to carry out the will of its parent company and the latter's intention and the intention of those directing it were also the intentions of the subsidiary; the same applied to the activities by which the deal was accomplished.

Californian Copper Syndicate v. Harris (1904) 5 T.C. 159; *Ducker v. Rees Roturbo Development Syndicate* [1928] A.C. 132, applied.

INCOME TAX APPEALS.

G. D. Watson for appellants.

D. A. Keith, Q.C. and *Bruce Verchere* for respondent.

THURLOW J.:—These are appeals from re-assessments of income tax which were heard together on common evidence pursuant to an order of the Court made prior to the trial. In the case of Construction Aggregates Corporation (hereinafter referred to as Construction Aggregates) the appeal is in respect of its 1962 taxation year. In the case of Sensibar Dredging Corporation Limited (hereinafter referred to as Sensibar Dredging), which is a wholly owned subsidiary of Construction Aggregates, the appeal is in respect of its 1961 taxation year. In both cases, however, the broad issue is whether the appellant is liable for income tax in respect of the same amount, a profit of $1,093,996.35 realized on or about June 23, 1961, in a transaction involving *inter alia* the sale to McNamara Suction Dredging Limited of a dredge known as the *Fleur de Lis.*

The Minister's position is that the amount in question is a taxable profit and that Construction Aggregates made the profit and is liable for the tax, but that if Construction Aggregates did not realize the profit Sensibar Dredging did realize it and is liable for tax in respect of it. Both appellants take the position that the profit was a capital gain but that if it is taxable it was Sensibar Dredging and not Construction Aggregates which realized the profit and is liable for the tax.

Construction Aggregates is a Delaware corporation which was incorporated in 1939 and since then has carried on a business formerly carried on by a predecessor corporation consisting mainly in dredging and land reclamation work. It also owns an area in the state of Michigan from which it produces sand and gravel which it processes and sells in the Great Lakes area. The dredging business is carried on in various parts of the world but principally in the United States. It includes the supplying under charter and the operating of dredges owned by Construction Aggregates in the performance of contracts for dredging work and it has included as well the performance of contracts for the designing and supervision of the construction of dredges for others and the operation of them for their owners on a fee basis. Under such a contract with Steep Rock Iron Mines Ltd., made in 1949 the company designed and supervised the building of two dredges and thereafter operated them in Canada for about twelve years for their owner. Under a further contract made in 1953 the company designed and supervised the building of another two dredges for Caland Ore Company Limited and operated them for that company for about nine years. And under a further contract made in 1954 the company designed and supervised the construction of the *Fleur de Lis* for Lake Asbestos of Quebec Limited (hereinafter referred to as Lake Asbestos), a subsidiary of American Smelting and Refining Company and thereafter operated it for its owner for about five years. In each of these cases from the point of view of the owner the purpose of the contract and operation was to secure the removal of underwater material so as to uncover ore bodies and in each case the contract contained a provision giving Construction Aggregates an opportunity to buy the dredge when no longer required by its owner at any price offered by another party which the owner would be prepared to accept. Until the events to be related these were the only operations ever carried out by Construction Aggregates in Canada.

In the case of the *Fleur de Lis* the work for which the dredge was designed and constructed was completed in September 1959 and shortly thereafter conversations took place which resulted in engineering personnel of Construction Aggregates preparing at the request of Lake Asbestos an estimate of the value of the dredge and the equipment associated with it. The estimate so produced was $828,000 and this was regarded by Lake Asbestos as a fair valuation though the evidence, so far as it goes, indicates that it was on the high side. In January 1960 a verbal understanding was reached that, subject to Lake Asbestos obtaining offers of a higher amount in the meantime, when Lake Asbestos was ready to dispose of the dredge Construction

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Aggregates might acquire it at the amount at which it had been valued less the value attributed to any portions of the equipment which Lake Asbestos might dispose of or decide to keep. Construction Aggregates thereupon began looking for work for the dredge in the course of which, in March 1960, it bid, unsuccessfully, on a substantial job to be done in Detroit. Later it negotiated with the International Nickel Company for the dredging work on a project at Thompson Lake in Manitoba but this fell through when the Nickel company deferred the project indefinitely. By mid-July another project was in the offing for work to be done near Quebec on a National Harbours Board project under a subcontract for dredging to be let by the Raymond International Company Limited (hereinafter referred to as Raymond), but it is not clear on the evidence whether Construction Aggregates knew of this job or not when near the end of July it received a letter from A. L. Quinlan the general manager of McNamara Marine Limited, one of a family of McNamara companies (hereinafter referred to as the McNamara organization), asking for an opportunity to discuss either at Chicago or elsewhere the possibility and means by which it might purchase one of the five dredges which had been or were being operated by Construction Aggregates for their owners in Canada on terms mutually satisfactory to both parties.

Thereafter on August 9 a conference took place at Chicago between Quinlan and Ezra Sensibar, the senior vice-president of Construction Aggregates, following which Sensibar circulated to several officials of Construction Aggregates a memorandum the first paragraph of which read as follows:

> His firm is interested in acquiring the "FLEUR DE LIS" and would like to work out something with us I told him that we had already reached an agreement in principle with AS&R under which we would buy the "FLEUR DE LIS" and were entirely agreeable to working out some joint arrangement with them and also that we did not close the door on an outright sale

The remainder, and by far the greater part, of the memo recites information which Sensibar obtained from Quinlan about the equipment held by a number of companies engaged in dredging in Canada. There is evidence that at this time Construction Aggregates regarded the opportunity for expanding its operations into eastern Canada to be favourable and intended to bid for Canadian jobs and to use the *Fleur de Lis,* when acquired, to do them. The *Fleur de Lis* was a 30 inch suction cutter dredge and was then at Black Lake near Thetford Mines in the Province of Quebec where it had been in use by Lake Asbestos. In order to use it elsewhere it would be necessary to dismantle, remove and rebuild it, which would be a substantial undertaking, but it seems to be common ground that once removed to the St. Lawrence River and rebuilt it would be far more efficient than any dredge controlled by competitors in eastern Canada from which I would suppose that it would put its possessor in a very favourable position to compete for work which it was capable of executing.

Save for a letter thanking Sensibar for his hospitality and saying that he, Quinlan, would write at a later date in the event that any concrete proposition could be made concerning the *Fleur de Lis* there was no further communication to or from the McNamara organization until the following January.

In the meantime Construction Aggregates bid for and obtained the Raymond subcontract to be performed by the use of the *Fleur de Lis,* arranged to buy the dredge from Lake Asbestos on a long term payment plan for $725,000 (this being the difference between $828,000 and the value of equipment disposed of or to be retained by Lake Asbestos) and prepared specifications for and called for bids for the work of dismantling, moving to the St. Lawrence River and rebuilding and refitting the dredge for work on the Raymond subcontract. Early in December Construction Aggregates learned that it would be necessary to have the dredge registered under the *Canada Shipping Act* and on December 30 instructed its Toronto solicitors to organize a Canadian subsidiary corporation the purpose of which was to be limited to a general contracting business with particular emphasis on dredging activities.

The subsidiary corporation, Sensibar Dredging, was incorporated under the *Companies Act*[1] on January 24, 1961, by letters patent which fixed its capital at $10,000 and stated its objects as being "to own and operate dredges and dredging equipment, apparatus and vessels and to

[1] R.S.C. 1952, c. 53.

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undertake and perform construction work and material moving contracts". By an agreement dated February 15, 1961, which recited that this company had been designated as the nominee of Construction Aggregates to take title to the dredge and equipment purchased from Lake Asbestos, Sensibar Dredging agreed with Lake Asbestos to assume the obligations of Construction Aggregates under the contract to purchase the dredge and equipment and by a bill of sale dated March 1, 1961, Lake Asbestos conveyed the dredge and equipment to Sensibar Dredging. Thereafter by a formal contract dated March 3, 1961 for the dredging work to be done near Quebec, Construction Aggregates, representing that it controlled the dredge, let it to Raymond under a charter arrangement in which Construction Aggregates agreed to provide the dredge and "all supervision, crew, master, labour, materials, fuel provisions, supplies, tools and equipment" and to perform the dredging work. In the meantime on January 24, 1961 Construction Aggregates had accepted by letter the tender of Geo. T. Davie & Sons Ltd. to dismantle, remove and rebuild the dredge for an amount somewhat in excess of $340,000. A formal contract for this work dated March 16, 1961 was later entered into by Construction Aggregates in its own name. The same company between February 2 and March 24 made three payments of about $34,000 each to the Davie company and on or about March 23 it also arranged for the issue of an irrevocable letter of credit from its banker to the Davie company to secure further progress payments totalling $241,980 all on account of the work being done or to be done on the dredge.

While these events were under way the McNamara organization in the fall of 1960 had been making a study of what would be required to dismantle, remove and rebuild the *Fleur de Lis* at Whitby, Ontario for its own purposes and on this basis had also made estimates of the value of the dredge at Black Lake, and of what amount it ought to be prepared to offer for it. I would infer from Exhibits V. 52 and A that it had intended to make its offer to Lake Asbestos but left it too late and then learned that Construction Aggregates had already bought the dredge. It does not appear that McNamara had heard at this stage of the Raymond subcontract or that it had been interested in bidding for it. On the other hand Construction Aggregates was not aware that the McNamara organization was engaged in making its study of the value of the dredge and of the costs of removing and refitting it.

Early in January 1961 George McNamara of the McNamara organization telephoned Ezra Sensibar and arranged to meet him on January 19 at the office of Construction Aggregates in New York. The meeting took place and, according to Sensibar, the gist of what occurred was that McNamara indicated that his organization was interested in some kind of a deal, preferably in buying the *Fleur de Lis*, and asked for a figure to discuss, that Sensibar told him that the figure would be based on cost of replacement which would be in the vicinity of $2,500,000, that Construction Aggregates was not interested in selling and preferred a joint project but that it was up to McNamara. McNamara indicated that he regarded the figure as unduly high. Sensibar's evidence is that his company was not in fact interested in selling the dredge and that it was reluctant but willing to consider joint operation or joint ownership.

About the middle of February McNamara called again and asked for another meeting. This was held in Chicago on February 28, when McNamara indicated that his organization continued to be interested in acquiring some ownership of the *Fleur de Lis*, but that he thought the price unreasonably high and suggested that a means of bridging the gap might be to combine his organization's equipment with the *Fleur de Lis* in a new company to be organized. The Construction Aggregates representatives were not much interested in this proposal, did not think the three small dredges owned by McNamara equivalent to the *Fleur de Lis* or that the scheme would be likely to be profitable and the meeting broke up to give the parties an opportunity to think about it and to meet again in Toronto. Sensibar and a Mr. Peebles, who was general counsel and a member of the executive committee of Construction Aggregates, met representatives of the McNamara organization in Toronto on March 7, were shown about their premises, decided that they did not wish to accept McNamara's proposal and so informed McNamara. McNamara was also informed that he still wished to buy the *Fleur de Lis*. Construction Aggregates was willing to do business at $2,400,000 but not otherwise.

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No written memo of what transpired at any of these meetings was made but there is evidence that the prices mentioned were for the dredge and associated equipment and did not include the Raymond subcontract.

Around the beginning of April, McNamara called again and a further meeting took place at Chicago on April 6 when several alternative propositions were discussed. A memo of these propositions was afterwards circulated and reads as follows:

> It was agreed that the McNamara interests are to have an option until April 30, 1961, to accept any one of four alternative propositions All of the propositions are based upon the complete "FLEUR DE LIS" dredge plant as it will be just before starting the Quebec contract (for Raymond International) or just after completing the work on the site. The plant will consist of the following
>
> a) The Dredge "FLEUR DE LIS".
> b) 1500′ of pontoon line
> c) 8000′ of 30″ shoreline.
> d) One derrick barge
> e) One cable reel barge together with cable
> f) Two tugs.
> g) One lot of spare parts and operating supplies and tools
> h) Six 1600 H.P G M diesel engines in the warehouse in Baltimore.
>
> The alternative propositions are as follows·
>
> 1 CAC will sell to McNamara the dredge plant together with the Raymond Sub-contract, before starting work, for $2,400,000 Sixty percent (60%) of this price is to be paid in cash and the remainder is to be paid by means of five serial notes bearing interest at the rate of five percent (5%), and due at one year intervals over a period of five years
>
> 2 CAC will sell to McNamara the dredge plant as above upon completion of the work under the Raymond contract or any extensions of it for $2,000,000 This is to be paid sixty percent (60%) in cash and the balance by means of five notes drawing interest at five percent (5%), and due at one year intervals over a period of five years.
>
> 3. McNamara and CAC will form a Canadian company which will buy the dredge plant, or the dredge plant and the Raymond contract McNamara will pay in sixty percent (60%) of the capital of this company and CAC will pay in forty percent (40%). The new company will buy the "FLEUR DE LIS" plant together with the Raymond contract just before work is commenced for the sum of $2,200,000 An agreement will be made between the parties so that either one may at any time post a price at which he would either buy or sell his stock. The other party will then have sixty (60) days during which he may exercise the right to buy or sell at this price. If he fails to act, then at the end of this period the first party must buy his stock.
>
> 4 The provisions under "3" above are modified only to the extent that the dredge plant will be purchased after the completion of the work at the Raymond site and the price would be $1,800,000

It was agreed that on or before April 30th, McNamara will notify CAC

a. That the deal is off;

or

b That it chooses one of the four alternative propositions

In the meantime McNamara may inspect the dredge in the George T. Davie Shipyard at Quebec

None of these propositions was ever accepted and Construction Aggregates did not even hear from McNamara until the middle of May when McNamara called by telephone and indicated that he wanted to take up the option even though it had expired and that he was ready to close on the basis of the purchase of the dredge with the Raymond subcontract immediately before the dredging was to begin, but that the price would have to be reduced to $2,000,000, that this was his final offer and that Construction Aggregates could either take or leave it, that there would be no further negotiations in the matter. A meeting was thereupon arranged for May 24 in Toronto when, after lengthy discussions, a deal was made and McNamara paid a deposit of $100,000. In essence, the deal was for the sale for $2,000,000 of the dredge with the Raymond subcontract as well, but not including one of the two tugs referred to in the memorandum of April 6 and not including as well the six diesel engines referred to in the memorandum. McNamara was given an option to purchase the diesel engines for an additional $200,000 but did not exercise it. Up to this time dredging in performance of the Raymond subcontract had not yet been started though expenses, referred to as "job costs" in the vicinity of $100,000 had been incurred in organizing and preparing to carry out the work. As part of the transaction, which purports to have been made between Sensibar Dredging and George McNamara on behalf of a company to be incorporated, McNamara agreed to pay these expenses and to assume responsibility for performance of the contract and in turn became entitled to the amounts payable by Raymond under it. The closing of the transaction was set for June 23 and it was provided that until that time Sensibar Dredging should perform the contract as agent for McNamara and should continue to perform it on the same basis thereafter in the event that Raymond should fail to consent to the assignment. On its part Sensibar Dredging undertook, subject to the consent of Raymond, to assign the contract

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and to cause Construction Aggregates to concur in such assignment. There is evidence that it had been intended to perform the dredging in the name of Sensibar Dredging, that an operating account and a payroll account had been opened in its name at a bank in Quebec and that the sign on the office on the job site bore that name but up to that time there had been no assignment to Sensibar Dredging of the contract or of the amounts to be paid by Raymond under it.

The transaction was finalized on or about June 23 when McNamara paid an amount of $840,000 together with certain adjustments on closing, assumed liability to the extent of $360,000 for the work done under the Davie contract in rebuilding the dredge and gave a mortgage on the dredge in favour of Sensibar Dredging to secure the remaining $700,000. The documents delivered included as well a bill of sale of the dredge from Sensibar Dredging to McNamara Suction Dredging Limited and assignments of the Davie and Raymond contracts. By the last mentioned assignment, in which Construction Aggregates joined, that company assigned the contract to McNamara Suction Dredging Limited, Sensibar Dredging assumed responsibility for the obligations of Construction Aggregates under it and McNamara assumed responsibility for the obligations of both Construction Aggregates and Sensibar Dredging under it. Thereafter the performance of the contract, which had been begun in the meantime on or about June 5 in the name of Sensibar Dredging, was undertaken by McNamara itself. Raymond, however, declined to release Construction Aggregates from its responsibility under the contract and did not formally consent to the assignment; though it appears to have been aware of the transaction and that the work was actually being done by McNamara it issued its cheques in payment for the work in favour of Construction Aggregates which thereupon endorsed them to McNamara. As part of the arrangements an engineer in the employ of Construction Aggregates continued to supervise the work at the expense of McNamara throughout the performance of the contract.

In the course of a year following the completion of this transaction Construction Aggregates acquired the dredges which it had been operating for Steep Rock Iron Mines Ltd. and Caland Ore Company Limited and still held all four of them at the time of the trial. Sensibar Dredging appears to have let to McNamara Suction Dredging Limited for a time the tug which had been excepted from the sale and to have earned some revenue therefrom and some interest on amounts belonging to it but it carried on no dredging or other business operations after the transaction in question and on May 15, 1962 its directors met and resolved that the company dispose of its property, distribute its assets rateably among its shareholders and proceed to wind up its affairs.

In the course of the argument counsel for the appellants as well as counsel for the Minister approached the matter, and suggested that I do so as well, by considering first the question whether the amount in question was income within the meaning of the *Income Tax Act* and thereafter the question of which of the two appellants, if either, is assessable in respect of it. However, while the answer in one case may be affected to some extent by the answer in the other, as I see it, the basic question in each case is whether the particular appellant realized a gain of the amount in question which in its hands was income for the purposes of the *Income Tax Act* and I have not found it convenient to consider the nature of that amount apart from the facts pertaining to the particular appellant. I propose therefore to consider first the nature of the gain on the assumption that it was realized by Construction Aggregates, thereafter the nature of the gain on the assumption that it belonged to Sensibar Dredging and finally the question which of the two should be regarded for the purposes of the *Income Tax Act* as having realized it.

The question with respect to the nature of the gain for the purposes of the *Income Tax Act* is whether the gain was profit from a "business" within the meaning of that term which, as defined in the Act, includes "a trade manufacture or undertaking of any kind whatsoever" and "an adventure or concern in the nature of trade". This issue is frequently stated as being whether profit realized from a transaction was income or a capital gain but while this may be a convenient way of posing it the relevent question for the purpose of the act is whether the profit arose from a business as defined in it. If so the profit is taxable as income whether or not by some standards it might be regarded as a capital gain. On the other hand if the profit

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is not profit from a business—and is not otherwise income—it matters not what name may aptly characterize it. The test to be applied for determining the question as propounded in *Californian Copper Syndicate v. Harris*[2] and as since applied in cases arising under the *Income Tax Act* is whether the gain in question was "a gain made in an operation of business in carrying out a scheme for profit making".

In the present case assuming that the profit from the transaction in question was realized by Construction Aggregates it appears to me to have been a profit that arose from and in the course of its business. As might be expected in a case such as this counsel for the appellants stressed the scope of the ordinary operating activities of Construction Aggregates, the nature of a dredge as capital equipment in that operation, that the *Fleur de Lis* was acquired for use in the business and that the transaction was a fortuitous and isolated one. These are undoubtedly matters to be weighed in determining the question but they are not inconsistent with the transactions from which the gain arose having been transactions of the appellant's business and there appear to me to be other features of the situation which taken together outweigh them and point to the conclusion which I have reached.

It is of course perfectly clear that a dredge may be an item of capital equipment for a person engaged in the dredging business and it is also clear that the *Fleur de Lis* might have become an item of capital equipment in the hands of Construction Aggregates if it had been held and put to use as such but the fact that it was acquired to some extent through Construction Aggregates having a right to do so obtained under a contract made in the course of its business together with the fact that the company had similar rights under two other contracts under which in due course, and possibly not very long afterwards, four other dredges might become available seems to me to militate against and to offset the *prima facie* character as capital equipment which a dredge in the hands of a corporation engaged in the dredging business, by its nature would otherwise suggest. In these circumstances the inten-

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[2] (1904) 5 T.C. 159.

tion with which the dredge was acquired appears to me to become particularly important. On the evidence I see no reason to doubt that Construction Aggregates in negotiating for the dredge did so with the intention, which it may well have had from the outset and no doubt had for some time before the Lake Asbestos dredging contract was completed, of acquiring the dredge for use in its business if it could do so on satisfactory terms. I see no reason to think, moreover, that it would not have acquired the dredge at or about the time when it did acquire it even if it had not in the meantime heard of or from the McNamara organization. The real state of Construction Aggregates purpose, however, is I think apparent from the memorandum which Ezra Sensibar wrote following his meeting with Quinlan on August 9, 1960. The company at that point appears to me to have intended to turn its rights with respect to the dredge and the dredge itself to account by acquiring and using or disposing of it in any way that might be likely to yield a satisfactory profit whether alone or in concert with others, which, as I see it, might have been done through a partnership or by selling the dredge to a company owned by the partnership or perhaps in other conceivable ways, or even by outright sale. There is evidence that resale of the *Fleur de Lis* was neither considered nor discussed by the directors of Construction Aggregates but there is also evidence that from that time on the possibility of working out terms for the outright sale of the dredge was in the mind of Ezra Sensibar, who appears to have been the person chiefly concerned on behalf of both appellants in the transactions in question, and in the minds of those to whom he reported. Nor do I see any reason to think that the purpose had changed by the time the contract to purchase the dredge was made even though by that time Construction Aggregates required it and intended to use it to perform the Raymond subcontract. The appellant's willingness to talk terms shortly afterwards to a person principally interested in purchasing rather than in any kind of joint venture together with the subsequent dealings between them appear to me to confirm that the intention of Construction Aggregates remained constant throughout. With respect to the appellant's inten-

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tion the situation seems to me to be the same in principle as that in *Ducker v. Rees Roturbo Development Syndicate*[3] where Lord Buckmaster said:

> Turning to the findings of the Commissioners, I find that they set out in detail the circumstances connected with the working of this company, and, in particular, the reports, which begin in 1907 and continue down to 1918. These reports show that the directors were contemplating from the beginning the possibility of the sale of some of these patents. It is quite true that they preferred not to sell them if a sale could be avoided, but the statement in para. 11 of the case is quite plain, that "the possibility of the sale of the foreign patents or rights has always been contemplated by the appellant company in respect of such interest as it possessed in the foreign patents". It is one of the foreign patents with which this appeal has to do, and the agreements, which are set out, showing the way in which the foreign patents in the case of France and of Canada have also been dealt with, show that that statement was not a statement of a mere accidental dealing with a particular class of property, but that it was part of their business which, though not of necessity the line on which they desired their business most extensively to develop, was one which they were prepared to undertake.

Next there is the fact that the considerations which influenced Construction Aggregates to make the deal were to my mind trading considerations. On this point, according to my note, Mr. Peebles said that there had been no change in value of the dredge from the time Construction Aggregates bought it in November 1960 until June of 1961 but that eastern Canada was regarded as an area in which dredging activity was developing rapidly, that the company intended to engage in dredging in that area and that it was important to keep the dredge out of the hands of a competitor. He went on to say that the reason for departure from the previous position was that the sale afforded Construction Aggregates the opportunity to arrive at a profit figure of $1,000,000 taxable at 25 per cent (in the United States) as a capital gain whereas they took into account that in operations one does not get continuity and assurance of profit and the opportunity to capture in a short time a capital gain profit of $1,000,000 was just too appealing.

The evidence of Mr. Ezra Sensibar is I think to the same effect. He said that in August 1960 on the occasion of his first conference with Mr. Quinlan he told Quinlan that Construction Aggregates had an agreement in principle to

[3] [1928] A.C. 132 at 141.

buy the dredge from Lake Asbestos, that their object was to go into the dredging business in eastern Canada which he regarded as an excellent market, that they regarded the *Fleur de Lis* as a most efficient dredge and had no special interest in selling but in operating it, that Quinlan pointed out that the McNamara organization could be of great help to Construction Aggregates because of their contacts and that he, Sensibar, said that Construction Aggregates would consider some sort of joint operation but had very little interest in selling. He also said that he knew very little about the competitive situation at that time, in fact had never heard of the McNamara organization, and that he took the opportunity to get the information about the dredges owned by the persons engaged in the business in Canada and to circulate it to his associates by the memo which he wrote. With respect to the reason for sale he said that it is not often they had an opportunity to earn $1,000,000 as a capital gain as a sure profit, that it took many years of successful hazardous operation to earn $2,000,000 which would be equivalent to $1,000,000 as a capital gain, and that the opportunity was more than they could resist. Viewed against the background of the company's widespread activities in the dredging business in various parts of the world, the considerations mentioned by the witnesses as the basis for their decision to sell the dredge and abandon the particular field to a competitor, appear to me to be distinctly related to the company's trading rather than to its capital structure, and this conclusion is, I think, enhanced when it is considered that a substantial trading contract which was regarded as being a valuable one was included in the deal.

Finally, the negotiations leading up to the transaction appear to me to be characteristic of trading rather than of mere realization of a capital asset. Counsel for the appellants pointed to the fact that it was McNamara throughout who was seeking a deal while Construction Aggregates was forging ahead with its plans to put the dredge to work in its business and that the deal ultimately made was unsought and unsolicited on the part of Construction Aggregates. However, the persons who represented Construction Aggregates in the negotiations, and particularly Mr. Ezra Sensibar, were skilled and experienced individuals with a wide knowledge of the dredging business as well as

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of the usefulness and value of dredges to persons engaged or proposing to engage in it. They were in a position to estimate and I think did estimate very well from time to time the strength of McNamara's determination to acquire or participate in the control of the *Fleur de Lis* and this I think put them in a position to suggest as a basis for negotiations a price far beyond what the dredge had cost their company. They then proceeded to yield somewhat from time to time whether by reduction of the price or otherwise. The price was first reduced from $2,500,000 to $2,400,000 for the dredge without the Raymond contract and later to $2,400,000 for the dredge with the Raymond contract or $2,000,000 without the contract. Though they suggested on the occasion in Toronto, when the McNamara proposal for a new company was rejected, that it was up to McNamara to purchase at their price or not as he wished, they nevertheless used the next occasion as one for further bargaining in which no less than four different propositions were made available to McNamara. Even after these had expired and McNamara had made a "take it or leave it" offer of $2,000,000 for the dredge and the Raymond contract they hammered out a deal at $2,000,000 for the dredge and the contract but not including some of the equipment included in the earlier offer. To my mind such activities are of the kind normally associated with trading with a view to profit.

I am accordingly of the opinion that, on the assumption that it was realized by Construction Aggregates, the amount in question was profit from that company's business and was income for the purposes of the *Income Tax Act*.

I turn now to the question whether the amount, assuming it to have been realized by Sensibar Dredging, was income in its hands. In this case as I view it the first consideration which I have mentioned in the case of Construction Aggregates does not apply since Sensibar Dredging was not party to and never did have any interest in the contracts by which Construction Aggregates obtained rights in respect of the purchase of the dredges which they had designed and operated for their owners. When, however, one comes to the question of the company's intention in

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assuming the purchase of the *Fleur de Lis,* notwithstanding the narrow expression of the objects of its incorporation contained in its letters patent, I see no reason to differentiate the intention of Sensibar Dredging from that which existed in the case of Construction Aggregates. The real object of Sensibar Dredging, as I see it, was to carry out the will of Construction Aggregates and the latter's intentions and those of the persons who directed it were also those of Sensibar Dredging. The same applies to the activities by which the deal was accomplished. This company had no previous or world-wide business activities which might have provided a setting or context by which the nature of the transaction might be determined but whether the acquisition and sale of the dredge and contract are regarded either with or apart from the events which preceded the company's incorporation in the light of its intention in acquiring the dredge at a time when a price had already been put on it in negotiations with McNamara and of the activities leading up to its disposition some two and a half months later the profit from the sale appears to me to have been one realized "in an operation of business in carrying out a scheme for profit making" and to have been income for the purposes of the *Income Tax Act.*

There remains the question which of these two corporations should be regarded for the purposes of the *Income Tax Act* as having realized the profit in question. There is, in my view, nothing in the evidence of what occurred prior to May 24, 1961, when the deal with McNamara was struck, which is necessarily inconsistent with the profit belonging to either. When offering by its letter of October 17, 1960 to buy the dredge Construction Aggregates proposed that it or a subsidiary would do so. Subsequently Construction Aggregates made the down payment and executed a formal contract to purchase. It subsequently designated Sensibar Dredging "as its nominee to take title" and that company by a formal contract with Lake Asbestos assumed responsibility for the purchaser's obligations to the vendor. Thereafter Construction Aggregates in its own name let the contract for the work to be done on the dredge and provided the financing therefor and it conducted the negotiations with McNamara as if Sensibar

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Dredging did not exist. In the circumstances, however, all this appears to me to be equivocal. Next there is the fact that the Raymond subcontract both initially and up to the time of the sale was in fact the contract of Construction Aggregates. On the other hand the evidence also shows that it was intended to have Sensibar Dredging perform it though on what basis is not clear and may, it seems, have been left undecided. There is also the fact that by the end of Sensibar Dredging's first fiscal period the bulk of the profit from the transaction was in the hands of Construction Aggregates and appears in the former's balance sheet as a debt owed to it by the parent company. On the evidence taken as a whole and on the last-mentioned features in particular there is I think something to be said for the submission on behalf of the Minister that Sensibar Dredging was a mere convenience and never did in fact own the dredge or realize the profit in question. On the other hand, there is evidence of Mr. Peebles, which I accept as reliable, that Sensibar Dredging was formed with the intention that it would hold title to the dredge and perform the Raymond contract. There is also evidence of Mr. Ezra Sensibar which I regard, as well, as reliable that the preliminary work at the site was carried out in the name of and for the account of Sensibar Dredging. There is also the fact that so far as appears Sensibar Dredging alone committed itself to and became party to the sale to McNamara and received the consideration. *Prima facie* this seems to me to indicate that the transaction which resulted in the profit in question was that of Sensibar Dredging and there does not appear to me to be anything in the evidence pointing unequivocally to the conclusion that the acts of Sensibar Dredging in connection with the transaction were or were intended to be in fact those of the parent company. There is also the consideration that as between a parent and its wholly owned subsidiary what is in fact to be done as the act of the subsidiary as distinguished from that of the parent is very much a matter of internal arrangement and of decision by the parent. In the present case the particular transaction from which the profit in question arose, besides being carried out in the name of the subsidiary appears from the audited statements attached to the income tax returns of both parent and subsidiary to have been treated as the transaction of Sensibar Dredging and I am unable to see any compelling reason why this should not be recognized. I shall therefore hold that the profit in question was realized by Sensibar Dredging.

In the case of Construction Aggregates the Minister's reply included a plea that that company had transferred to Sensibar Dredging its right to receive the consideration for the dredge and was liable for tax in respect of the profit from the transaction under section 16(1) of the Act. At the trial this plea was neither pressed nor abandoned but in view of the conclusion I have reached that the transaction from which the profit arose was Sensibar Dredging's there is, in my opinion, no scope for the application of section 16(1).

The appeal of Sensibar Dredging therefore fails and it will be dismissed with costs. In the circumstances the course taken by the Minister of assessing both appellants and contesting both appeals was in my opinion a proper one and the costs to be paid by Sensibar Dredging will include the Minister's costs in the Construction Aggregates appeal.

The appeal of Construction Aggregates will be allowed without costs and the re-assessment will be referred back to the Minister to be revised in accordance with these reasons.

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Dec. 5

Dec. 12

BETWEEN:

BENSON & HEDGES (CANADA) LIMITED .... APPELLANT (*Opponent*);

AND

ST. REGIS TOBACCO CORPORATION .... RESPONDENT (*Applicant*);

AND

THE REGISTRAR OF TRADE MARKS.

Trade marks—Opposition to registration—Whether confusion between marks—Appeal from Registrar's decision—Whether Registrar proceeded on wrong principle or exercised discretion judicially—Whether defence of invalidity open—Trade Marks Act, R.S.C. 1952, c. 291, ss. 6, 12(1)(d), 16(3), 19, 37.

Appellant, owner of the trade mark "Gold Band", which had been registered for use in association with the sale of cigars, cigarettes, etc., used the mark in association with the sale of cigars since 1928. In 1966 following an application by respondent for registration of the trade mark "Golden Circlet" for use in association with the sale of cigarettes appellant filed an opposition to such registration under s. 37 of the *Trade Marks Act* on the ground that the proposed mark was confusing with appellant's mark. The Registrar of Trade Marks rejected the opposition. On appeal to this court the parties relied solely on the evidence filed with the Registrar.

Held, although in the court's view there was confusion between the two marks the appeal must be dismissed because it had not been shown that in coming to the opposite conclusion the Registrar proceeded on a wrong principle or that he failed to exercise his discretion judicially. *Rowntree Co. v. Paulin Chambers Co.* [1968] S.C.R. 134 applied.

Held also, where an opposition is filed under s. 37 on the ground of confusion with a registered trade mark it is not open to the respondent to attack the validity of the registration (as respondent did here by contending that appellant had abandoned its design mark and its word mark for use in association with cigarettes).

APPEAL from decision of Registrar of Trade Marks.

J. C. Osborne, Q.C. for appellant.

Donald F. Sim, Q.C. and *R. H. Hawkes* for respondent.

JACKETT P.:—This is an appeal under section 55 of the *Trade Marks Act*, chapter 49 of the Statutes of Canada of 1952-53, from a decision of the Registrar of Trade Marks under section 38 of that Act allowing an application by the respondent for registration of the trade mark "GOLDEN CIRCLET" to be used in association with "cigarettes".

The appellant, who had filed a statement of objection to the respondent's application under section 37 of the *Trade Marks Act*, is the registered owner of a design trade mark consisting of the words "Gold Band" between two black lines on a gold background, which was registered on September 13, 1928. This trade mark was originally registered to be used in connection with the sale of cigars. The registration was amended on June 9, 1942 so as to include cigarettes and tobaccos of every kind and description. The appellant is also the registered owner of a word trade mark consisting of the words "Gold Band" in respect of "cigars, cigarettes and tobaccos of every kind and description" which was registered on September 12, 1958, at which time it was shown as having been used in Canada since 1928.

The appellant has used the trade mark "GOLD BAND" in association with the sale of cigars in all parts of Canada and has so used that trade mark since 1928. There is some evidence that at one time it also sold cigarettes under the trade mark "GOLD BAND", but the evidence as to that is not at all precise. The appellant has advertised cigars under the trade name "GOLD BAND" extensively in Canada.

On April 11, 1964, the respondent filed with the Registrar of Trade Marks its application to register the trade mark "GOLDEN CIRCLET", stating that it intended to use the trade mark in Canada in association with cigarettes. There is no evidence that it has, as yet, ever used that trade mark.

By its statement of opposition, the appellant opposed the respondent's application on several grounds of the various kinds contemplated by section 37(2) of the *Trade Marks Act*. Counsel for the appellant has, however, made it clear that the only grounds that need to be considered are

(a) that the trade mark "GOLDEN CIRCLET" is not registrable because it is confusing, within the meaning of section 6 of the *Trade Marks Act*, with the appellant's registered trade marks to which I have

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referred and is therefore not a "registrable" trade mark by reason of section 12(1)(*d*) of that Act, and

(b) that the respondent is not the person entitled to registration of the trade mark "GOLDEN CIRCLET" because that trade mark is confusing, within the meaning of section 6 of the *Trade Marks Act,* with the trade mark "GOLD BAND", which had been previously used in Canada by the appellant, and the respondent does not, therefore, fall within the provision contained in section 16(3) of the *Trade Marks Act.*

The relevant parts of sections 12 and 16 read as follows:

12. (1) Subject to section 13, a trade mark is registrable if it is not

* * *

(*d*) confusing with a registered trade mark; or

* * *

16. (3) Any applicant who has filed an application in accordance with section 29 for registration of a proposed trade mark that is registrable is entitled, subject to sections 37 and 39, to secure its registration in respect of the wares or services specified in the application, unless at the date of filing of the application it was confusing with

(*a*) a trade mark that had been previously used in Canada or made known in Canada by any other person;

The provisions of the Act that govern the determination of the question so raised as to whether the respondent's proposed trade mark, "GOLDEN CIRCLET", is confusing with the appellant's registered trade marks or the trade mark that it had used in Canada are to be found in section 6, which reads in part:

6. (1) For the purposes of this Act a trade mark or trade name is confusing with another trade mark or trade name if the use of such first mentioned trademark or trade name would cause confusion with such last mentioned trade mark or trade name in the manner and circumstances described in this section.

(2) The use of a trade mark causes confusion with another trade mark if the use of both trade marks in the same area would be likely to lead to the inference that the wares or services associated with such trade marks are manufactured, sold, leased, hired or performed by the same person, whether or not such wares or services are of the same general class.

* * *

(5) In determining whether trade marks or trade names are confusing, the court or the Registrar, as the case may be, shall have regard to all the surrounding circumstances including

(*a*) the inherent distinctiveness of the trade marks or trade names and the extent to which they have become known;

(*b*) the length of time the trade marks or trade names have been in use;

(*c*) the nature of the wares, services or business;

(*d*) the nature of the trade; and

(*e*) the degree of resemblance between the trade marks or trade names in appearance or sound or in the ideas suggested by them.

At this stage, I should mention a contention of the respondent that the appellant could not rely on its registered design mark and could not rely on its word mark except as used in association with cigars because it must be taken to have abandoned them inasmuch as the design mark had not been used by the appellant for at least twelve years and the word mark had not been used except in association with cigars for at least twelve years. His contention was that, in an infringement action, it was clear that a defence of invalidity could be raised as against a registered trade mark and that there was, therefore, no reason why the same contention could not be raised when a registered mark is relied on in an opposition to registration of another trade mark. In my view, this contention fails.[1] There is a clear contrast, from this point of view, between section 19 of the Act and section 37 read with section 12(1)(*d*). Section 19 says that registration of a trade mark in respect of any wares gives to the owner the exclusive right to its use throughout Canada in respect of such wares "unless shown to be invalid". Section 37(2) says that an application for registration may be opposed on, *inter alia*, the ground that "the trade mark is not registrable" and section 12(1)(*d*) says, in effect, that a trade mark is not registrable if it is "confusing with a registered trade mark". I can only conclude that, while in an action in the Court for infringement the defendant is entitled to challenge validity, when an application is made to the Registrar for registration of a new mark, he is not to register it as long as a confusing trade mark is on the register. If the registration of an invalid trade mark is interfering with registration of a new trade mark, the applicant can take the necessary steps to have the register corrected.

Both parties filed evidence with the Registrar and no new evidence was adduced in this Court. The evidence

[1] I must not be taken as finding that the alleged abandonment was established by the evidence.

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upon which the respondent relied before the Registrar is summarized in his written argument as follows:

> It was admitted by Mr Secter in his cross-examination that many cigars on sale in Canada, both those manufactured in Canada and those imported, have a gold band around them. Reference is made to Exhibits 1 to 6 inclusive to Mr Secter's cross-examination which illustrated that this is the case and to Mr. MacGowan's affidavit of December 22nd, 1965 filed on behalf of the applicant which indicates that for at least the last twenty-seven years and at the present time many cigars with gold bands around them have been on sale in Canada. Samples are also attached as exhibits to Mr. MacGowan's affidavit.
>
> Particular reference is directed to the House of Lords cigar filed as Exhibit 5 to Mr Secter's cross-examination. This cigar not only has a gold band or stripe on the container but is actually referred to as a "Gold Stripe" cigar. Mr. Secter made it clear in his cross-examination that his company made no objection to this use and intended to make no objection to this use.
>
> It is also clear from the exhibits that many packages of cigars have a gold band or gold stripe on them of one sort or another.
>
> The evidence also makes it clear that a number of cigarettes and cigarette packages at present in use in Canada have a gold band either on the package or on the cigarette. Reference is made to Exhibits 7, 8 and 9 to Mr. Secter's cross-examination. The Peter Jackson pack has a gold band extending around it. The Filter Player's package of Exhibit 8 has a strip or band of gold around the package and the Player's Filter King cigarettes have a gold stripe line or band around the cigarettes themselves.
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> * * *
>
> So far as concerns the nature of the trade, it is respectfully pointed out that by Mr Secter's own admission no company in Canada uses the same trade mark as applied to both cigars and cigarettes This will be found in Mr. Secter's cross-examination on pages 8 to 10. This is a fact well known to purchasers of cigars and cigarettes who, it is also submitted, tend to be mutually exclusive. Having regard to the nature of the trade, it is submitted that no person who is assumed to be familar with the opponent's "Gold Band" cigars would possibly think he was buying the opponent's product if he purchased the applicant's "Golden Circlet" cigarettes.

That part of the appellant's written argument that refers to the evidence reads as follows:

> Evidence in support of the opponent was filed by way of two Affidavits by Joseph Secter, the Secretary-Treasurer of the opponent company, both Affidavits being taken on May 10, 1965 In the longer Affidavit, Mr. Secter clearly states the use of his Company's trade mark GOLD BAND, in particular, he states that in the past five years, his Company has sold in Canada under its trade mark GOLD BAND in excess of 28,000,000 cigars, having a wholesale value in excess of $2,000,000 To Mr. Secter's Affidavits are attached specimens of his Company's trade mark GOLD BAND as used in association with cigars and also one of his Company's specimen cartons showing the trade mark GOLD BAND as used in association with cigars.

Mr. Secter's shorter Affidavit, also dated May 10, 1965, places on record specimens of advertising by his Company with respect to the trade mark GOLD BAND.

On May 10, 1965, Mr. Secter was cross-examined under oath, in terms of Rule 46(2) of the Trade Marks Act, by Learned Counsel for the applicant. Mr Secter in his replies made it as clear as possible that his Company, Benson & Hedges (Canada) Limited had taken no action against the manufacturers of the House of Lords cigars, nor against the manufacturers of Peg Top cigars, because the trade marks used by both manufacturers in association with their cigars do not stress that their marks are "gold band labels". Mr. Secter, time and again, reiterated his point which can be seen, for example, in his answer on Page 27 of the transcript of the cross-examination. He says, in reply to being asked whether it is not a common practice for manufacturers of cigars to use a gold band around cigars "no, they use a band around the cigars which may contain many things, gold and red and blue and yellow or some other colour, but they do not stress that it is a "gold band" label That is the problem"

Mr Secter was shown a package of Peter Jackson king size filter cigarettes, referred to as Exhibit 7 on Page 31 of the transcript This package had on it a tear strip consisting of a gold line Mr Secter referred to this as a mechanical device to take care of what is called the cellophane around the package and, in his answer at the foot of Page 31 of the transcript, he states in effect that cigarette packages have this device only for removing the cellophane and the device may be of gold or another colour. He states "it has nothing to do with the brand"

On December 22, 1965, an Affidavit was taken by Mr Wallace G MacGowan, wholesale representative of Rothman's of Pall Mall Canada Limited of Toronto, Ontario. To this Affidavit are attached specimens of cigar bands, marked Exhibits "A" to "O" which comprise gold bands. Mr. MacGowan confirms that cigar bands are being constantly changed by manufacturers and is therefore unable to say over what period any cigar band covered by Exhibits "A" to "O" has been on the market

On March 4, 1966, a further Affidavit was taken by Mr Secter pursuant to Rule 45 of the Trade Marks Act, this Affidavit being in reply to that taken by Mr MacGowan, referred to above. Mr. Secter admits that many cigar bands contain the colour gold but, once again, he maintains that his company's trade mark registrations contain the words "gold band" and such registrations are valid and are subsisting. Mr. Secter also states that his Company did at one time sell cigarettes under its trade mark GOLD BAND but does not do so at the present time. This does not imply that his Company will not recommence the production and sale of cigarettes under its trade mark GOLD BAND Mr. Secter referred, when under cross-examination, to the fact that in the tobacco trade use of trade marks is what is known as cyclic, that is to say, trade marks are used for some years and then are retired but are subsequently used again for a further number of years This appears to be the practice of manufacturers of cigars, tobacco and cigarettes Mr. Secter also refers to the fact that certain manufacturers sell both cigars and cigarettes under the same trade mark.

In Paragraph 9 of his Affidavit, Mr. Secter states that if a purchaser asked for a cigar sold under the trade mark GOLD BAND, the purchaser will be offered a cigar which is manufactured and sold

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by his Company and the same purchaser will not be offered a cigar around which is a gold band with the reading matter House of Lords or White Owl. In Paragraph 10 of Mr. Secter's Affidavit, he states quite clearly that his Company makes no claim to the colour gold, which is common to the trade, but his company does have rights in the trade mark GOLD BAND because this trade mark consists of the words "gold band" and is not merely a cigar band of gold colour. In Paragraph 11 of his Affidavit, Mr. Secter states that in his opinion, the use of the mark GOLDEN CIRCLET in respect of cigarettes in Canada would lead to confusion in the minds of the purchasing public on account of his Company's trade mark GOLD BAND.

By his decision dated March 30, 1967, which is the decision appealed from, the Registrar set out the grounds upon which the appellant opposed the application and then disposed of the opposition as follows:

> I have duly considered the evidence and the written arguments filed by both parties. Neither party requested a hearing. Having regard to the circumstances of the case on the basis of the evidence adduced, I have come to the conclusion that the grounds of opposition are not well founded. The marks are sufficiently different in appearance, in sound and in the ideas suggested by them to preclude confusion within the meaning of Section 6 of the *Trade Marks Act*.
>
> The opposition is accordingly rejected pursuant to section 37(8) of the *Trade Marks Act*.

Having regard to section 6(2) of the *Trade Marks Act*, the question that the registrar had to decide is whether the use of the trade mark "GOLDEN CIRCLET" and the use of the trade mark "GOLD BAND" in the same area "would be likely to lead to the inference that the wares ...associated with such trade marks are manufactured...by the same person" whether or not such wares are of the same general class. In reaching his conclusion, he was bound to follow the direction in section 6(5), which I repeat for convenience:

> (5) In determining whether trade marks or trade names are confusing, the court or the Registrar, as the case may be, shall have regard to all the surrounding circumstances including
>
> (a) the inherent distinctiveness of the trade marks or trade names and the extent to which they have become known;
>
> (b) the length of time the trade marks or trade names have been in use;
>
> (c) the nature of the wares, services or business;
>
> (d) the nature of the trade; and
>
> (e) the degree of resemblance between the trade marks or trade names in appearance or sound or in the ideas suggested by them.

Giving all due weight to the decision of the Registrar, who, I realize, has had infinitely more experience in this very specialized field than I have had, when I have regard to all the surrounding circumstances, including

(a) the fact that the trade mark "GOLD BAND", while it is not what is apparently referred to as a strong mark, had, before the respondent's application, become very well known in Canada, and the fact that the trade mark "GOLDEN CIRCLET" was not known at all,

(b) the fact that the trade mark "GOLD BAND" had been used in Canada for at least six years before the application was made, and the fact that the trade mark "GOLDEN CIRCLET" has not been used at all,

(c) the fact that cigars and cigarettes are closely related wares,

(d) the fact that the wares in question are ordinarily sold by the same retailer over the same counter, and

(e) the fact that there is very substantial resemblance between the trade mark "GOLD BAND" and the trade mark "GOLDEN CIRCLET" (when they are considered on a first impression basis and not by way of a detailed comparison) in appearance, sound and the ideas suggested by them,

I cannot escape the conclusion that if those two trade marks were used in the same area it would be very likely to lead to the inference that the wares associated with them were manufactured by the same person and thus that, by virtue of section 6(1), the one is "confusing" with the other for the purposes of the *Trade Marks Act.*

If, therefore, it were my duty on this appeal to come to a conclusion as to what the Registrar should have decided, and to substitute my conclusion for his if I come to a different one, I would allow this appeal.

I have, however, come to the conclusion that it is not open to me, in the circumstances of this case, to substitute my conclusion for that of the Registrar, having regard to the nature of this Court's duty on an appeal of this kind as established by the decision of the Supreme Court of Canada

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in *The Rowntree Company Limited v. Paulin Chambers Co. Ltd. et al.*[2] In that case, as in this, there was an appeal from a decision of the Registrar on an application for registration of a trade mark. In that case, this Court substituted its view on an issue as to whether two trade marks were confusing for that of the Registrar, there was an appeal to the Supreme Court of Canada, and that Court, by a unanimous judgment delivered by Ritchie J., allowed the appeal and restored the Registrar's decision. The part of the reasons for judgment which, as I understand it, contain the reasoning by which the Court reached its decision, is the following:

> It is contended on behalf of the respondent that the conclusion reached by the learned trial judge should not be disturbed having regard to the terms of s 55(5) of the Act which provides that "on the appeal... the Court may exercise any discretion vested in the Registrar". I do not, however, take this as meaning that the Court is entitled to substitute its view for that of the Registrar unless it can be shown that he proceeded on some wrong principle or that he failed to exercise his discretion judicially[3]
>
> * * *
>
> In my view the Registrar of Trade Marks in the present case applied the test required of him by the statute and I do not think that grounds were established justifying the learned judge of the Exchequer Court in interfering with his conclusion. For all these reasons I would allow this appeal and restore the decision of the Registrar of Trade Marks refusing the respondent's application S N. 264951.

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[2] [1968] S.C.R. 134.

[3] For a very similar approach, see *Union Carbide & Carbon Corporation's Application*, (1952) 69 R P C. 306, per Lloyd-Jacob J. at page 308, where he said:

> "If I were satisfied that in arriving at that decision the Hearing Officer had observed the right approach, having regard to the language of the Statute and the guidance given by the decided cases, the mere fact that his conclusion would not necessarily be that at which I myself would have arrived without his assistance is no reason whatever for interfering with his decision. Indeed, I think it would be true to say that, even if I came to the conclusion, as I think I might, that his conclusion was fanciful, and indicated failure to appreciate the unsubstantial nature of the objection posed, none the less, except upon the footing that in exercising his discretion the Hearing Officer had failed to exercise it judicially, I should not be justified in interfering with his conclusion. Accordingly I have given the closest attention to the language in which he has framed his conclusion and indicated his mental process, in order that I should be in a position to determine whether or not there has been any departure from the principles which it is incumbent upon those dealing with these matters to bear fully in mind."

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In this case, no submission has been made that the Registrar proceeded on a "wrong principle" or "that he failed to exercise his discretion judicially" and I know of no basis upon which any such submission could have been made. Not only is there no indication that he failed to follow the requirements of any provision in the statute, but there is no room for suggesting that he left out of account any material fact[4] or came to any conclusion on the facts that could not be supported on the evidence. Certainly, there is no room for suggesting that he did not act judicially. That being so, there is no occasion for this Court to interfere with his conclusion and substitute its decision for his.

The appeal is dismissed with costs.

[4] Presumably the situation would be different if, under section 55(5) of the *Trade Marks Act*, additional evidence were adduced in this Court that made a difference of substance between the facts before the Registrar and the facts before this Court. Compare *The Queen v. Secretary of State*, [1953] 1 S.C.R. 417, per Locke J. at pages 425-6.

Vancouver 1967 Dec. 18
1968 Jan. 15

BETWEEN:

GEORGIA GULF ESTATES LTD. APPELLANT;

AND

THE MINISTER OF NATIONAL REVENUE .... RESPONDENT.

Income tax—Capital gain or business profit—Company acquires hotel, improves operations and sells—Whether adventure in nature of trade—Tests for determining.

Appellant, which was controlled by two men, was incorporated with the object of acquiring and operating hotels. Another company controlled by the same two men had previously bought a hotel, effected improvements with the object of increasing the hotel's profits and its value, and then sold it in August 1959 through a real estate broker at a profit. In January 1960 the last-mentioned company purchased a hotel for $330,000, transferred it in November 1960 to appellant, effected improvements in its operation, listed it with real estate brokers in 1961 at a sale price of $440,000, and eventually sold it in January 1962 for $426,000

Held, the profit on the sale was from an adventure in the nature of trade, and therefore taxable, because (1) appellant bought the hotel with the intention of selling it at a profit (*Campbell v. M.N.R.* [1953] 1 S.C R. 3, *Regal Heights v M N.R.* [1960] S C.R 902, *DeToro v. M N R.* [1965] 2 Ex C R 715, *Willumsen v M.N R.* [1967] 2

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Ex. C.R. 257); (2) the listing of the hotel with real estate brokers and the various dealings with the brokers were operations of the same kind and carried on in the same way as those which were characteristic of ordinary trading in the line of business in which the venture was made (*Irrigation Industries Ltd. v. M.N.R.* [1962] S.C.R. 346); and (3) the sale of the hotel following active steps to improve its operation indicated that the transaction was that of an ordinary trader or dealer in hotels (*M.N.R. v. Taylor* [1956-1960] Ex. C.R. 3).

INCOME TAX APPEAL.

P. N. Thorsteinsson and *M. J. O'Keefe* for appellant.

S. A. Hynes for respondent.

SHEPPARD D.J.:—This appeal is by Georgia Gulf Estates Ltd. against an assessment of the 17th June, 1966, by the Minister holding that the taxable income for the taxation year 1962 included the profit on the resale of the Marine Hotel at Westview, adjoining Powell River, B.C., which the appellant contends was in error in that such profit was capital gain realized from the sale of an investment. The facts follow.

On the 19th July, 1955, Tudor Holdings Ltd. bought Tudor House in Esquimalt for $100,000 and on the 1st August, 1959 sold it for $265,000. The Tudor Holdings Ltd. had three shareholders, but the third was bought out so that thereafter the issued shares in Tudor Holdings Ltd. and in the appellant when subsequently incorporated were held by Hutchinson 200 shares and by Higbie 100 shares.

In January, 1960, Tudor Holdings Ltd. purchased the Marine Hotel at Westview, B.C. for $330,000 and on the 22nd November, 1960, Tudor Holdings Ltd. transferred to the appellant that day incorporated, and thereupon the Tudor company was wound up. On the 1st January, 1962, the appellant sold the Marine Hotel for $426,000; that is the transaction in question. On the 11th June, 1962, the appellant bought Westholme Hotel, Victoria, B.C. for $335,000 which it renovated and has since operated as the Century Inn. On the 17th June, 1966, the appellant was assessed by the Minister on its profit on the sale of the Marine Hotel at Westview.

Upon notice of objection the Minister on the 20th July, 1966, confirmed the assessment and the appellant brought this appeal on the ground that the profit was not income but capital derived from the realization of a capital asset. The issue raises the problem whether the appellant was engaged at the appropriate time in the business of buying and selling hotels so that the transaction in question comes within the *Income Tax Act*, sections 3 and 4, particularly as extended by section 139(1)(*e*) to include "an adventure or concern in the nature of trade", the contention of the Minister; or whether the transaction was the realizing of a capital asset as contended by the appellant.

In *Irrigation Industries Ltd. v. M.N.R.*[1], the appellant taxpayer abandoned its original purpose of incorporation and purchased 4,000 shares of 500,000 in another company which it later resold at a profit. It was held the purchase was an investment and the sale was the realizing of capital and not of taxable income. Martland J. stated the test and their application as follows:

at p. 352:

> The positive tests to which he refers as being derived from the decided cases as indicative of an adventure in the nature of trade are: (1) Whether the person dealt with the property purchased by him in the same way as a dealer would ordinarily do and (2) whether the nature and quantity of the subject-matter of the transaction may exclude the possibility that its sale was the realization of an investment, or otherwise of a capital nature, or that it could have been disposed of otherwise than as a trade transaction.
>
> I will deal first with the second of these tests, which, if applied to the circumstances of the present case, would not, in my opinion, indicate that there had been an adventure in the nature of trade.
>
> The nature of the property in question here is shares issued from the treasury of a corporation and we have not been referred to any reported case in which profit from one isolated purchase and sale of shares, by a person not engaged in the business of trading in securities, has been claimed to be taxable.
>
> Cases in which the nature and quantity of the property purchased and sold have indicated an adventure in the nature of trade include *The Commissioners of Inland Revenue v. Livingston* ((1926), 11 Tax Cas. 538) (a cargo vessel); *Rutledge v. The Commissioners of Inland Revenue* ((1929), 14 Tax Cas. 490) (a large quantity of toilet paper); *Lindsay v. The Commissioners of Inland Revenue* ((1932), 18 Tax Cas. 43) and *Commissioners of Inland Revenue v. Fraser* ((1942), 24 Tax Cas. 498) (a large quantity of whisky); *Edwards v. Bairstow* ([1960] A.C. 14) (a complete spinning plant) and *Regal Heights Ltd. v. Minister of National Revenue* ([1960] S.C.R. 902) (40 acres of vacant city land).
>
> Corporate shares are in a different position because they constitute something the purchase of which is, in itself, an investment.

[1] [1962] S.C.R. 346.

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They are not, in themselves, articles of commerce, but represent an interest in a corporation which is itself created for the purpose of doing business. Their acquisition is a well-recognized method of investing capital in a business enterprise.

and at p. 353:

Furthermore, the quantity of shares purchased by the appellant in the present case would not, in my opinion, be indicative of an adventure in the nature of trade, as it constituted only 4,000 out of a total issue of 500,000 shares.

In the second test, the emphasis is put on the subject-matter of the transaction, hence if the subject matter can be properly used only by resale, then the purchase and resale are presumed to have been "an adventure or concern in the nature of trade". To the judgments cited there may be mentioned *M.N.R. v. Taylor*[2], where 1,500 tons of lead requiring 22 carloads to carry, were bought and resold by the taxpayer to his company. Thorson P. at p. 30 said:

The nature and quantity of the subject matter of the transaction were such as to exclude the possibility that it was other than a transaction of a trading nature. The respondent could not do anything with the lead except sell it and he bought it solely for the purpose of selling it to the Company. In my judgment, the words of Lord Carmond in the *Rheinhold* case (*supra*) that "the commodity itself stamps the transaction as a trading transaction" apply with singular force to the respondent's transaction.

In the first test the emphasis is put on the party to the transaction and his conduct. That test is elaborated as follows: *Irrigation Industries Ltd. v. M.N.R.*, (*supra*), by Martland J. at p. 354:

"...whether a venture such as we are now considering is, or is not, 'in the nature of trade', is whether the operations involved in it are of the same kind, and carried on in the same way, as those which are characteristic of ordinary trading in the line of business in which the venture was made." That covers all the cases.

citing *Leeming v. Jones*[3] and continues at p. 354:

Were the operations involved in the present case of the same kind and carried on in the same way as those which are characteristic of ordinary trading in the line of business in which the venture was made?

and later at p. 354:

But it may be contended that persons may make a business merely of the buying and selling of securities, without being traders

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2 [1956-60] Ex C R. 3.
3 [1930] 1 K B. 279 at p. 283.

in securities in the ordinary sense, and that the transactions involved in that kind of business are similar, except in number, to that which occurred here.

In *M.N.R. v. Taylor*, (*supra*), Thorson P. at p. 29 said:

> But there are some specific guides. One of these is that if the transaction is of the same kind and carried on in the same way as a transaction of an ordinary trader or dealer in property of the same kind as the subject matter of the transaction it may fairly be called an adventure in the nature of trade. The decision of the Lord President in the *Livingston* case (*supra*) and the *Rutledge* case (*supra*) support this view. Put more simply, it may be said that if a person deals with the commodity purchased by him in the same way as a dealer in it would ordinarily do such a dealing is a trading adventure: *vide* Lord Radcliffe's reasons for judgment in *Edwards v. Bairstow* (*supra*).

As to profits—in *Irrigation Industries Ltd. v. M.N.R.* (*supra*), Martland J. stated at p. 350:

> It is difficult to conceive of any case, in which securities are purchased, in which the purchaser does not have at least some intention of disposing of them if their value appreciates to the point where their sale appears to be financially desirable.

at p. 354:

> ... where the realization of securities is involved, the taxability of enhanced values depends on whether such realization was an act done in the carrying on of a business.

at p. 355:

> The only test which was applied in the present case was whether the appellant entered into the transaction with the intention of disposing of the shares at a profit so soon as there was a reasonable opportunity of so doing. Is that a sufficient test for determining whether or not this transaction constitutes an adventure in the nature of trade? I do not think that, standing alone, it is sufficient.

In *M.N.R. v. Taylor*, (*supra*), Thorson P. stated at p. 26:

> The intention to sell the purchased property at a profit is not of itself a test of whether the profit is subject to tax for the intention to make a profit may be just as much the purpose of an investment transaction as of a trading one.

and at p. 30:

> It is of no avail to the respondent that when he purchased the lead he did so without any intention of selling it to the Company at a profit. He did not pretend that his purchase was for an investment purpose. All his reasons were business reasons of a trading nature. His adventure was a speculative one. ... He saw advantages of a business nature in the transaction...

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It follows that purchasing with the intent to resell at a profit is not an exclusive nor absolute test as it does not prevent the transaction being the realization of an investment and not taxable income as in *Irrigation Industries Ltd. v. M.N.R.*, nor does the absence of such intent to resell at a profit preclude the transaction being an "adventure ... in the nature of trade" and the proceeds taxable income as in *M.N.R. v. Taylor*, (*supra*). But where the transaction falls within either of the two tests, buying with intent to resell at a profit may be applied, as for example, where a person who owns properties or commodities deals with them in the same way as a dealer, then he is engaged in an "adventure ... in the nature of trade" within section 139(1)(*e*) and any profit is taxable income. The test of purchase with intent to resell at a profit was applied in the following judgments: *Campbell v. M.N.R.*[4]; *Regal Heights Ltd. v. M.N.R.*[5]; *DeToro v. M.N.R.*[6]; *Willumsen v. M.N.R.*[7].

Those tests lead to the question whether the circumstances here are those required to bring the transaction in question within section 139(1)(*e*). That is essentially a question of fact: *Campbell v. M.N.R.*, (*supra*) per Locke J. at p. 6; *McIntosh v. M.N.R.*[8]. The appellant contends that it bought the Marine Hotel solely to be operated as a hotel and for no other reason; on the other hand, the Minister contends that the appellant bought the hotel to operate and by increasing the revenue thereby to increase the value and to sell at a profit. That question of fact is the ultimate issue.

As to the facts of this case, the memorandum of association (Ex. A-1) of the appellant company has the objects of acquiring and operating hotels and of operating the particular parts thereof, which objects also imply the power to sell so as to make a profit: *The Companies Act*, R.S.B.C. 1960, c. 67, sec. 22(1) empowers the company to carry on any business capable of being conveniently carried on or to enhance the value or render profitable any of the proper-

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[4] [1953] 1 S C R. 3 per Locke J. at pp. 6, 7.
[5] [1960] S C.R. 902 per Judson J. at p. 905.
[6] [1965] 2 Ex. C R. 715 per Cattanach J. at p. 728.
[7] [1967] 2 Ex. C.R. 257; 67 DTC 5022 per Cattanach J. at p. 5028.
[8] [1958] S.C.R. 119 per Kerwin C.J.C. at p. 121.

ties and rights of the company, (p), to sell and deal with property and rights of the company (q), and to do all things incidental (x).

Further, there was throughout a system to buy a hotel, to improve and to sell at a profit. Hutchinson and Higbie were experienced in operating the Tudor House and Hutchinson had a cost accounting system which imposed a continuous check of each department to see if it were paying. Their purpose, in the Tudor Company and in the appellant, was to buy a hotel in which the management could be improved, and to increase the revenue and thereby increase the value.

(1) In each instance they bought a hotel which could be improved. The Tudor House was not operating successfully. Hutchinson told Marriette that they had renovated the hotel, doubled the area of the beer parlour, paved the parking lot, thereby making it a profitable operation. They listed with Enterprise Realty and sold at a profit.

(2) After the sale Hutchinson looked at hotels as he wanted an integrated hotel operation and eventually chose the Marine Hotel as the management could be improved, it was not of the best. Hutchinson reviewed the operating profits of the hotel by departments and introduced a cost accounting system. The appellant by Hutchinson and Higbie discharged all the kitchen help which had formerly been causing trouble by taking leave in a group, renovated the dining room at a cost of $30,000, and the food department alone developed a profit of $30,000. In March or April, 1961, Hutchinson told Marriette that his (Hutchinson's) cost accounting was responsible for making the hotel a desirable picture, and that he intended to put it up for sale.

(3) In the case of the Tudor House the Tudor Company, and in the case of the Marine Hotel the appellant, increased the operating profits and sold the hotel at a profit, and in the case of both companies Hutchinson and Higbie were shareholders with control.

Throughout there was the intention of increasing the profits so as to increase the value; that was stated by Hutchinson. But if the intention were only to operate the

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hotel as a capital asset, then it was no concern of the taxpayer or of the shareholders that there was an increase in value. The purpose of increasing the value could indicate the intent to sell as a primary purpose. In each case the company did sell at a profit.

As to listing—both the Tudor House and the Marine Hotel were listed with real estate agents for the purpose of sale. The Tudor House was listed with the Enterprise Realty Company and a commission paid on the sale. Early in 1961, not later than August 1961, the appellant listed the Marine Hotel with Gillanders Realty of Vancouver by an oral listing exclusive for sixty days for sale at $440,000 to realize a net sum of $425,000. Hutchinson on behalf of the appellant went to the office of Gillanders Realty in Vancouver to see what other hotels were for sale, and there gave the oral listing specifying the price. That listing indicates that at least that early the appellant, having acquired the hotel in November 1960, had decided not to profit by operating but by selling, and that the improvements then made and consequent operating profit had permitted a net asking price of $425,000. In August of 1961 Hutchinson made an oral arrangement with one Marriette, and Marriette produced Mantoani as the agent of the syndicate who ultimately purchased at $426,000. Further, some real estate agents specialize in selling hotels, and listing to them is a common method of selling hotels. Hence that listing would indicate dealing with the hotel in a way or "characteristic of ordinary trading" in hotels, within *Irrigation Industries Ltd. v. M.N.R.*, (*supra*), and dealing "as a dealer would ordinarily do" within *M.N.R. v. Taylor*, (*supra*).

After the sale was completed the appellant refused to pay any commission beyond the $1,000. There was an action for commission, initially by Marriette Agencies Ltd. and later amended to Hopper & Jamieson Limited, of which action there were put in as exhibits an examination for discovery of Hutchinson (Ex. R-3), the proceedings at trial (Ex. R-4) and the reasons for judgment of Wootton J. (Ex. A-5). At that trial (Ex. R-4, p. 3) Hutchinson testified that he gave a listing to Gillanders Realty at $440,000 and testified, "Yes, I told him that I wanted $425,000 net to Georgia Gulf Estates and that we wanted cash to the mortgage".

In the reasons for judgment (Ex. A-5) Wootton J. held:

> I find upon the facts that the witness Marriette was the instrument of introduction of the purchaser to the defendant...(p. 2)
>
> It was the witness Marriette, an unlicensed person, who "found the purchaser" and he secured the purchaser. As I indicated above, these acts he could not perform as the basis for the claim of commission. (p. 6)
>
> Apparently there were some visits by Hutchinson to the office of the plaintiff and some casual talk between Creamer and Hutchinson over the telephone and once at the airport...
>
> ... Very little was done beyond naming the person interested in the purchase of the hotel and the delivery of one or two statements.
>
> Upon the whole of the evidence and after considering the law and the arguments raised I am of the opinion that the plaintiff has failed to prove its case in any part and I therefore dismiss the action with costs. (pp. 7-8)

Here the question is not whether there was a valid listing within the *Real Estate Act,* R.S.B.C. 1960, c. 330, Sec. 4, but in this action the question is whether there were such conduct of the appellant through Hutchinson as would indicate, in relation to the Marine Hotel, an "adventure or concern in the nature of trade" within Section 139 (1)(*e*)—that is, whether such conduct was "characteristic of ordinary trading" within *Irrigation Industries Ltd. v. M.N.R.*, (*supra*), or such "as a dealer would ordinarily do" such dealing within *M.N.R. v. Taylor*, (*supra*), and not whether there were a valid listing. In such purported listing in "fixing the price" and in resale, it cannot be said that the role of the appellant was passive or "the antithesis of what one would expect from a vendor under like circumstances": *M.N.R. v. Valclair Investment Company Ltd.*[9].

The onus is on the appellant to prove error in the assessment: *Dezura v. M.N.R.*[10]. The weight of the evidence of Hutchinson, the sole witness for the appellant, is affected by his answers on the examination for discovery in this action, wherein he said the appellant did not make any efforts to sell the Marine Hotel. In question 71 he stated:

> 71. Q. What efforts did the Appellant make to dispose of the Marine Hotel?
> A. I did not make any efforts.

That answer may be contrasted with his evidence on examination for discovery in the action of *Hopper and*

[9] [1964] Ex. C.R. 466, Kearney J. at p. 477.
[10] [1948] Ex. C.R. 10.

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Jamieson Limited v. Georgie Gulf Estates Limited (Ex. R-3) in which he stated he did grant a listing, as follows:

14. Q. Are you referring to an interim agreement dated December 5th, 1961?
    A. Yes, I am.
15. Q. But presumably the decision to place the hotel for sale was reached prior to that date. Is that right?
    A. Well, it would have been sold prior to that date if we had come to some agreement, yes.
16. Q. And prior to that date did you place the hotel for sale with anyone other than the plaintiff?
    A. It was listed at one time, yes.
17. Q. And who did you list it with?
    A. An outfit called Gillanders Realty, here in town.
18. Q. Here in Vancouver?
    A. Yes.
19. Q. When was the hotel listed for sale with that company?
    A. Oh, it would be in the early part of 1961. I can't recall just exactly when it was.
20. Q. Did the defendant company give that company an exclusive listing?
    A. It was an oral exclusive listing. I had done business with this outfit before.
21. Q. What price if any did you instruct them to find a purchaser for?
    A. We were asking for $425,000 00 net to Georgia Gulf Estates.
22. Q. And did you discuss with that company what commission if any would be paid if a purchaser would be found at that price?
    A. No. Gillanders Realty decided to list the hotel at the price of $440,000.00.
23. Q. Were they successful in selling the hotel?
    A. No, they weren't.
24. Q. Did you subsequently ask anyone else to attempt to sell the hotel?
    A. No, I did not.

* * *

88. Q. Well, do you recall what you did say?
    A. The hotel was always for sale but it wasn't really on the market. I'll put it that way.
89. Q. But did you not express concern to Mr. Marriette or Mr. Creamer at the delay in the Mantoani syndicate coming up with a firm offer?
    A. Well, there was no firm offer. There never was a firm offer until—

Hutchinson's answers on discovery in *Hopper and Jamieson Limited v. Georgia Gulf Estates Limited* offer difficulty to saying that his evidence alone in this present action in the light of the unexplained absence of Higbie is of sufficient weight to shift the onus of proof.

In January 1960, Hutchinson and family went to Powell River and, according to Hutchinson, "They were very unhappy after a very short time" because of the isolation and small size of the community. In November 1960, Tudor Company conveyed to the appellant. On that evidence there would have been an intention to sell before the appellant acquired the hotel, but in any event, assuming such dissatisfaction with Powell River and Westview, that does not necessarily exclude the prior intention to make a subsequent sale as an adventure in the nature of trade within section 139(1)(*e*).

The appellant has cited the following judgments. The appellant contended that the proceeds of the Marine Hotel should be regarded as capital for the reasons in *Irrigation Industries Ltd. v. M.N.R.*, (*supra*). There the appellant bought 4,000 shares in a company out of the 500,000 shares which were issued, and resold at a profit. Martland J. at p. 352 stated:

> Corporate shares are in a different position because they constitute something the purchase of which is, in itself, an investment. They are not, in themselves, articles of commerce, but represent an interest in a corporation which is itself created for the purpose of doing business. Their acquisition is a well-recognized method of investing capital in a business enterprise.

and at p. 355:

> In my opinion, the transaction in question here does not fall within either of the positive tests which the authorities have suggested should be applied.

That judgment is distinguishable in the subject matter; there "corporate shares", here a hotel.

Sterling Paper Mills Inc. v. M.N.R.[11] is also distinguishable on the facts. There the appellant bought a paper mill admittedly intending to operate it as a capital investment but the vendor refused to sell the mill without selling with it a timber limit. It was held that the timber limit became a capital asset, and the sale at a profit was the realizing of a capital asset. That judgment is distinguishable on the

[11] [1960] Ex. C.R. 401.

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facts as the purchaser was there required to purchase by the vendor, and there was here a voluntary purchase by the appellant with a view to resale at a profit.

The appellant cited *Hazeldean Farm Company Limited v. M.N.R.*[12] as authority for the principle that to bring the transaction within section 139(1)(*e*) there must be at the time of purchase an intent to resell at a profit. The judgment establishes no such principle for the following reasons:

(1) That principle contended for did not arise as the only question raised was the intent at the time of purchase. Noël J. at p. 617 states:

> ... was the appellant's intention as far as the balance of the land was concerned, exclusively to farm it, or had it a dual intent as suggested by counsel for the respondent of holding this land and developing it until it became ripe for profitable disposition and in the interim deriving some income from some farming activities and rental of the property.

It was not necessary to consider a later intent as that point was not raised.

(2) The principle contended for by the appellant is not the law. It is open to an owner to convert at any time a capital asset into a business inventory so as to make the resale an "adventure or concern in the nature of trade" within section 139(1)(*e*).

In *Irrigation Industries Ltd. v. M.N.R.* (*supra*), Martland J. stated at p. 354:

> ... where the realization of securities is involved, the taxability of enhanced values depends on whether such realization was an act done in the carrying on of a business.

In *Moluch v. M.N.R.*[13] the taxpayer bought land, used it as a home and farm and later subdivided and sold lots. Cattanach J. said at p. 718:

> There is no doubt whatsoever in my mind that when the appellant originally acquired the land in question he did not do so with an intent to turn it to account for profit by selling it. This fact was readily conceded by counsel for the Minister in presenting his argument. However, even if, at the time of acquisition, the intention of turning the lands to account by resale was not present, it does not necessarily follow that profits resulting from sales are not assessable to income tax. If, at some subsequent point in time, the appellant embarked upon a business using the lands as inventory in the

[12] [1967] 1 Ex. C.R. 245; [1966] C.T.C. 607.
[13] [1967] 2 Ex. C.R. 158; [1966] C.T.C. 712.

business of land subdividing for profit, then clearly the resultant profits would not be merely the realization of an enhancement in value, but rather profits from a business and so assessable to income tax in accordance with Sections 3 and 4 of the *Income Tax Act*, R.S.C. 1952, chapter 148.

In *M.N.R. v. Firestone Management Limited*[14] Jackett P. at pp. 774-5 approved the *Moluch* case in the following words:

> The appellant relies on the recent decision of my brother Cattanach in *Moluch v. M.N.R.*, [1966] C.T.C. 712, in which it was decided that the appellant had acquired land as a *capital asset* of a farming business and, after he ceased carrying on that business, used that land as the *inventory* of a new business in which the raw land was converted into building lots and made the subject matter of an operation of selling lots to individual builders. I entirely agree with that decision and I also agree with Cattanach J. that, in any particular case, "the matter is one of degree depending upon the business-like enterprise and activity displayed." I also agree that an "element of trade" would be introduced if a purchaser were, by himself or his own employees, or by a contractor, through an expenditure of effort and monies, to change the character of the property. Whether such "element of trade" is such as to constitute the particular operations the carrying on of a business remains, as Cattanach J. says, a question of degree "depending upon the business-like enterprise and activity displayed".

(3) In any event here the appellant did purchase with the intention of selling the hotel at a profit. Whether there is such an intent is a question of fact on which there may be diversity of opinion: *Scott v. M.N.R.*[15] and being a question of fact is outside the doctrine of *stare decisis*.

In conclusion, here there is an adventure in the nature of trade within section 139(1)(*e*) for the following reasons:

(1) The appellant purchased the Marine Hotel with the intention of selling at a profit: *Campbell v. M.N.R.*, (*supra*), Locke J. at pp. 6, 7; *Regal Heights Ltd. v. M.N.R.*, (*supra*), Judson J. at p. 905; *DeToro v. M.N.R.*[16]; *Willumsen v. M.N.R.*, (*supra*), Cattanach J. at p. 5028.

(2) The listing at a fixed price and various visits with Marriette are operations of the same kind and carried on in the same way as those which are characteristic of ordinary trading in the line of business in which the

[14] [1967] 1 Ex. C.R. 340; [1966] C.T.C. 771 at 774.
[15] [1963] S.C.R. 223, Judson J. at p. 225.
[16] [1965] 2 Ex. C.R. 715, Cattanach J. at p. 728.

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venture was made: *Irrigation Industries Ltd. v. M.N.R.*, (*supra*), at p. 354, namely, in the business of selling hotels.

(3) The sale of the hotel through the active efforts of Hutchinson, which included Hutchinson's assuming the office of general manager and his installing a system of cost accounting over all departments, the improvement in the hotel, in the operating profits and in the value of the hotel, the listing by the appellant with Gillanders Realty and fixing the sale price, the subsequent similar transactions with Marriette which resulted in the sale at $426,000, all these indicate the transaction as being of the same kind and carried on in the same way as a transaction of an ordinary trader or dealer in property of the same kind: *M.N.R. v. Taylor* (*supra*), at p. 29, that is, of an ordinary trader or dealer in hotels.

The appeal is therefore dismissed with costs.

Montreal 1967

Dec. 12, 14-15

Ottawa 1968 Jan. 26

BETWEEN:

D.W.S. CORPORATION ....APPELLANT;

AND

THE MINISTER OF NATIONAL REVENUE ....RESPONDENT.

Income tax—Deductions—Money borrowed and loaned to subsidiary—Whether used to earn income from business or property of parent company.

Income tax—Deductions—Foreign exchange premium in payment of long-term indebtedness on trading account—Consistency of accounting practice.

In 1959 appellant, which was in the business of manufacturing, etc. whiskey, borrowed $3,485,000 from a Canadian subsidiary at 6% per annum and advanced that sum to a U S subsidiary on a demand note without interest to enable the latter company to finance the purchase of a large quantity of unmatured Scotch fillings for maturing in Scotland over a period of years In 1963 the U.S. subsidiary transferred the Scotch fillings to appellant and paid appellant $10,000 as remuneration for the loan In its tax returns for 1960, 1961 and 1962, appellant claimed a deduction of the interest paid on the borrowed money.

On August 31st 1961, the last day of its 1961 fiscal year, appellant (as a result of a suggestion by the income tax authorities) paid an indebtedness of $3,051,000 in U.S. funds, the balance owing a U.S.

supplier on whiskey and other items of a current nature purchased over a period of several years. This indebtedness had been recorded at par in appellant's accounts. The Canadian dollar had for years been above par in terms of U.S. dollars but declined to below par during appellant's 1961 fiscal year and appellant was obliged to pay a premium of $96,364 to obtain the U.S. dollars required. In its 1961 tax return appellant claimed a deduction of the premium so paid. Prior to this transaction appellant's accounting practice had been to record purchases and sales in U S. dollars at the prevailing exchange rate for Canadian dollars and when subsequently making payment to record any change in the amount of Canadian dollars required.

Held, allowing the appeal in part:

1. The interest paid was not deductible because the borrowed money was not used to earn income either from appellant's business or from its property as required by s. (11)(1)(*c*) of the *Income Tax Act*. *Canada Safeway Ltd. v. M.N.R.* [1957] S C.R. 717, applied

2. The foreign exchange premium was deductible in computing appellant's income for 1961 because (a) it was paid in that year in satisfying a loss on trading account in accordance with the accounting method appellant had been following, and because (b) it was a loss sustained on trading account in 1961 as a result of the decline of the Canadian dollar and which was merely measured by the transaction of August 31st 1961 *Eli Lilly & Co. (Can) Ltd. v. M.N.R.* [1955] S C.R. 745; *Tip Top Tailors Ltd. v M.N R.* [1957] S C R 703; *Can. Gen. Elec. Co. v. M N R* [1962] S C R. 3, referred to.

INCOME TAX APPEAL.

Jacques M. Tétreault for appellant.

Alban Garon and *Pierre H. Guilbault* for respondent.

THURLOW J.:—This is an appeal from re-assessments of income tax for the years 1960, 1961 and 1962. In respect of each of these years there is in issue the claim of the appellant to deduct, in the computation of its income for income tax purposes, the interest paid by the appellant on an amount of $3,485,000 borrowed by it on September 4, 1959 from Caus Investment and Finance Company Limited, a subsidiary of the appellant, allegedly for the purpose of earning income from the appellant's business. The Minister's position on this issue is that the borrowed money was not used to earn income from the appellant's business or property but was used to finance the operations of World T. and I. Corporation, another subsidiary of the appellant.

Issues were also raised on the right of the appellant to deduct interest paid on a further amount of $185,000 borrowed by the appellant from Caus Investment and Finance

Company Limited on September 4, 1960 and on a further amount of $180,000 borrowed by the appellant from Caus Investment and Finance Company Limited on September 4, 1961 but the evidence showed that these two borrowed amounts were used as working capital in the appellant's business and the Minister's case with respect to the deductibility of the interest thereon was abandoned by counsel in the course of the argument. The appeal on these issues accordingly succeeds.

In respect of the year 1961 there is a further issue as to the right of the appellant to deduct a loss of $96,364 on foreign exchange which is alleged to have been incurred in paying to Schenley Industries Inc., of which the appellant is a subsidiary, a debt payable in United States funds for inventories, supplies and other items of a current nature. On this issue the Minister's position is that the loss was not a business loss deductible from income under the provisions of section 12(1)(*a*) but was a loss on account of capital the deduction of which is prohibited by section 12(1)(*b*) of the *Income Tax Act.*

The material before the Court on both of the issues which remain to be determined consists in part of admissions contained in the notice of appeal and reply and in an agreed statement of facts and in part of oral and documentary evidence adduced in the course of the trial.

The appellant was incorporated in 1945 under the *Companies Act* of Canada by the name of Canadian Schenley Limited and since then has carried on the business of distilling, aging, blending, bottling, labelling and selling Canadian whiskeys and on occasion buying and selling other spirits. During the years here in question its business was carried on only in Canada. The name of the appellant was changed to D.W.S. Corporation in 1964.

World T. and I. Corporation is a foreign corporation organized in 1959 with its principal office in New York. During the years in question it was engaged in the business of buying Canadian whiskeys from the appellant and selling them in the United States and elsewhere, other than in Canada, and of buying and selling throughout the world certain types of whiskeys distilled in the United States and Scotch whiskeys which it matured itself or which it purchased as matured whiskeys.

Caus Investment and Finance Company Limited was incorporated under the *Companies Act* of Canada and was an investment company.

The immediate object of the transactions of September 4, 1959 was to arrange the financing of the purchase by World T. and I. Corporation in Scotland of an exceptionally large quantity of unmatured Scotch fillings. These, it was intended, would remain in Scotland for several years during which the maturing process would be going on and warehousing and other costs would be accumulating and when withdrawn from the warehouse would be blended and imported into the United States and there bottled and sold. In the transactions in question the appellant borrowed $3,485,000 in United States funds from Caus Investment and Finance Company Limited, which was evidenced by a promissory note payable on demand with interest at six per cent and thereupon advanced the amount so borrowed together with an additional $15,000 in United States funds derived from other sources to World T. and I. Corporation which used it to pay for the Scotch fillings. The loan to World T. and I. Corporation was also evidenced by a demand promissory note which was dated at New York and was silent as to interest. A journal entry of the appellant dated September 1959, which was offered in evidence (Exhibit 4) without oral explanation or elaboration as to how it came to be made or who made it, recorded the borrowing of $3,321,641 by the appellant from Caus Investment and Finance Company Limited and the loaning of it to World T and I. Corporation with the following explanation:

> To record portion of demand loan receivable from World T & I and demand loan payable to Caus Investment resulting from the loan by Caus to Cdn Schenley of $3,485,000 U.S. Funds which in turn was loaned by Cdn Schenley to World T & I Corp. Loan of $3,485,000 U.S. Funds converted at 4 11/16 to arrive at $3,321,641. Loan from Caus bears 6% interest, loan to World T & I is non-interest bearing.

In 1963, as a result of a change, the precise nature of which was not explained, in the revenue laws of the United States applicable to World T. and I. Corporation a decision was made to transfer the ownership of the Scotch fillings to the appellant and in August of that year this was done, some of the fillings being transferred to the appellant in

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satisfaction of the loan obligation, others as a dividend in kind and the remainder by a reduction of the capital of World T. and I. Corporation. Thereafter the fillings were disposed of by the appellant over a period of years and the appellant thus became the recipient of the revenues from their sale.

In the latter part of 1963 a payment of $10,000 as remuneration for the use of the borrowed money was made by World T. and I. Corporation to the appellant pursuant to an agreement set out in a letter from the appellant to World T. and I. Corporation dated August 26, 1963 the body of which read as follows:

> Reference is made to conversations which we have had relating to your demand loan from us, dated September 4th, 1959, in the principal amount of $3,500,000.00, and its repayment on August 19th, 1963. We have concurred that this note, being payable on demand, bore no other fixed date of maturity. Also, no reference to interest payable on said note was indicated thereon, it having been mutually agreed at time of issuance that this might be a subject for discussion at a later date and the subject of a later agreement.
>
> As stated above, you have discharged the principal amount of said indebtedness on August 19th, 1963. Furthermore, we now confirm that you shall compensate us in full for the use of this money by paying to us, in addition to the above-mentioned principal amount of $3,500,000 00, interest in the amount of $10,000.00. We also confirm that our receipt of said payment of $10,000 00 shall discharge in full your obligations arising out of said demand note. For reasons given by you, this payment of $10,000.00 will not become due until November 1st, 1963, and we hereby confirm our agreement to this arrangement.
>
> Please acknowledge your concurrence in this determination by signing and returning the enclosed copy of this letter.

In the same month of August 1963 Caus Investment and Finance Company Limited was wound up and the indebtedness of the appellant to it was extinguished on the distribution of its assets to the appellant as its sole shareholder. In each of the years 1960, 1961 and 1962, however, the appellant had paid Caus Investment and Finance Company Limited an amount in the vicinity of $200,000 as interest on the loan and it is the deductibility of these sums in computing the appellant's income for tax purposes that is in issue.

I should add at this point that there is evidence given by Mr. Arthur W. Gilmour, a chartered accountant, who as financial adviser and consultant on Canadian tax matters to the Schenley companies participated in meetings of senior officers of the appellant and its parent company, that the senior officers of the various subsidiary companies of the Schenley group were jealous of the profit showings of the companies for which they were responsible and that it was the policy of the senior officers of the parent company to allocate revenues to each subsidiary company so that it would be able to reflect in its profit and loss statements its fair share of the profits or losses arising from ventures to which more than one of them had in some way contributed. He went on to say that at the time of the making of the loan to World T. and I. Corporation no decision had been made as to whether the fillings would be marketed in the United States by that company and that no decision had been made with respect to a rate of interest to be paid for the use of the money since the venture in purchasing the whiskey was hazardous and its results were not predictable. He expressed himself as sure, however, that had World T. and I. Corporation held the fillings to maturity and marketed them the appellant would have pressed in the councils of the organization for interest for the use of the money over the lengthy period involved. The witness also said that at one point during the currency of the loan he was asked to make a report on the reasons for the reduced state of the appellant company's earnings which reduction was in part due to the fact that it was receiving no income from the use of the borrowed money but was paying interest on its own loan from Caus Investment and Finance Company Limited at six per cent and that when the decision was made that the fillings should be transferred to the appellant it was considered that since the appellant would be receiving the revenues from the marketing of the fillings it would be amply reimbursed for the use of the money during the time it was on loan to World T. and I. Corporation and that the president of the appellant was well satisfied that the arrangement afforded satisfactory remuneration therefor. Mr. Gilmour also said that it was intended at the time of the making of the loan that interest would be charged though the amount or rate could not then be determined and that it was he who recommended in 1963 that the token payment of $10,000 as remuneration be paid.

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In the view I take of the matter the transaction in which the exceptional quantity of Scotch fillings was purchased was entirely that of World T. and I. Corporation for its own account and there was at that time neither any agreement for sharing with the appellant any profits or losses that might arise from the venture nor any agreement to remunerate the appellant for the use of the money loaned to it over the rather lengthy period for which it would be required whether at a particular rate of interest or at interest the rate or amount of which would be determined later or at all. The appellant as the owner of all the shares of World T. and I Corporation was no doubt in a position to determine what World T. and I. Corporation would do, and might either by the exercise of that power or by demanding payment of the loan put World T. and I. Corporation in a position where it could not successfully decline to pay interest but in the way matters stood throughout the relevant period there was as between the two corporations no right accruing to the appellant to interest or to any other kind of remuneration. On this point I regard it as being of some significance that in referring in his letter of August 26, 1963 to what occurred at the time of the loan on the subject of interest the president of the appellant company stated that it was agreed that interest might be a subject for discussion at a later date and the subject of a later agreement and did not use an unequivocal expression indicative of an agreement at that time that remuneration in some form was to be paid. This to my mind falls short of saying that it was intended at the time either that interest at some rate was to be paid or that interest was to be charged. It is also of significance that no decision had been made as to who would market the fillings when they were matured and that no rate of interest had been determined. This to my mind indicates that the whole subject of remuneration for use of the money was in abeyance and that no decision had been made that any remuneration would be allocated or paid.

Moreover, Mr. Gilmour's statement that it was intended at the time that interest would be charged suffers both from the fact that it was made in response to a leading question put by counsel for the appellant and even more from the fact that it is an expression by the witness of a conclusion as to what was in someone else's mind rather than a statement of known facts from which the Court might draw a conclusion one way or another on the critical point. To my mind this is not acceptable as evidence of what in fact was intended. Even if it were acceptable as evidence of someone's intention—the witness did not say whose intention it was—there is a difference between someone's intention to charge interest at some undetermined rate at some later time and a present arrangement between a prospective payor and payee that interest at some reasonable rate having regard to circumstances and relevant considerations will be paid. Here there is, in my view, no evidence of any such arrangement binding World T. and I. Corporation during the relevant period to pay anything whatever as remuneration for use of the borrowed money.

In a case of this kind, that is to say, one in which the taxpayer is not engaged in a business which itself involves the borrowing of money and the payment of interest thereon, the deductibility of interest in computing income for tax purposes turns on section 11(1)(*c*) of the *Income Tax Act* by which it is provided that:

> 11.(1) Notwithstanding paragraphs (*a*), (*b*) and (*h*) of subsection (1) of section 12, the following amounts may be deducted in computing the income of a taxpayer for a taxation year:
>
> (*c*) an amount paid in the year or payable in respect of the year (depending upon the method regularly followed by the taxpayer in computing his income), pursuant to a legal obligation to pay interest on
>
> (i) borrowed money used for the purpose of earning income from a business or property (other than borrowed money used to acquire property the income from which would be exempt),
>
> . . .
>
> or a reasonable amount in respect thereof, whichever is the lesser;

For the purpose of determining the present issue the critical words of the section are "borrowed money used for the purpose of earning income from a business or property" and the question which they raise is whether in the circumstances described the $3,485,000 in United States funds which the appellant borrowed from Caus Investment and Finance Company Limited on September 4, 1959 was in the years 1960, 1961 and 1962 *used for the purpose of earning income from* (the appellant's) *business or property*

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when, throughout the material period, the borrowed money remained on loan to the appellant's subsidiary, World T. and I. Corporation, with no agreement in effect under which remuneration for the use of the money was being earned or would be or become payable.

So far as the appellant's claim to deduct the interest may be based on the submission that the borrowed money was used for the purpose of earning income from the appellant's business the matter, in my view, is concluded against the appellant by the judgment of the Supreme Court in *Canada Safeway Limited v. M.N.R.*[1]. In that case the appellant sought to deduct interest on borrowed money used to purchase shares and thus to acquire control of a company which was one of its suppliers. By securing control of this company the appellant was able to obtain trading advantages over competitors which resulted in enhanced profits from the appellant's business. The Court, however, held the interest on the borrowed money not deductible not alone because the dividends from the shares would constitute exempt income but also because the borrowed money was not used in the appellant's business. With respect to the 1947 and 1948 taxation years, to which the *Income War Tax Act* applied, Kerwin C.J. speaking for himself and Taschereau J. (as he then was) said at page 723:

> Reliance was placed upon subs. (1)(*b*) of s. 5, but the exemption and deduction there contemplated of "such reasonable rate of interest on borrowed capital used in the business to earn the income as the Minister in his discretion may allow" do not apply, first, because the money borrowed on the debentures was not used by the appellant in its own business to earn the income and . . .

Reference was then made to sections 11, 12 and 27 and 127(1) of the 1948 *Income Tax Act* and the learned judge observed at page 724:

> Generally speaking, these enactments have the same effect as those applicable to the 1947-1948 taxation years and, if anything, the definitions included in the *Income Tax Act* clarify the situation.

Rand J., referring to section 11(1)(*c*)(i), said at page 728:

> The language in (i) "used for the purpose of earning income from a business" corresponds with that of s. 5(1)(*b*) of the repealed Act and to what has been said on the latter there is nothing to be added: the business of the subsidiary is not that of the company.

[1] [1957] S.C.R. 717.

Earlier Rand J. had said at page 727:

> It is important to remember that in the absence of an express statutory allowance, interest payable on capital indebtedness is not deductible as an income expense. If a company has not the money capital to commence business, why should it be allowed to deduct the interest on borrowed money? The company setting up with its own contributed capital would, on such a principle, be entitled to interest on its capital before taxable income was reached, but the income statutes give no countenance to such a deduction. To extend the statutory deduction in the converse case would add to the anomaly and open the way for borrowed capital to become involved in a complication of remote effects that cannot be considered as having been contemplated by Parliament. What is aimed at by the section is an employment of the borrowed funds immediately within the company's business and not one that effects its purpose in such an indirect and remote manner.

I shall therefore hold that the borrowed money here in question was not during the relevant period *used for the purpose of earning income from* (the appellant's) *business* within the meaning of section 11(1)(*c*) of the Act.

The submission was, however, made that the borrowed money was used for the purpose of earning income from the appellant's property, that is to say, the demand note given by World T. and I. Corporation or the property right which it evidenced. It was not suggested that the money was used for the purpose of earning income in the form of dividends from World T. and I. Corporation but I do not think such a contention would be tenable anyway since such dividends, if received, would, I think, be income from the appellant's property in the shares of World T. and I. Corporation rather than from the property right evidenced by the demand note. On this point Rand J. in *Canada Safeway Limited v. M.N.R.* said at page 728:

> The word "property" is introduced in paras. (i) and (ii) but I cannot see that it can help the appellant: the language
>
> *borrowed money used for the purpose of earning income from ... property (other than property the income from which is exempt)*
>
> in (i) means the income produced by the exploitation of the property itself. There is nothing in this language to extend the application to an acquisition of "power" annexed to stock, and to the indirect and remote effects upon the company of action taken in the course of business of the subsidiary.

Though in the present case there was no use of the borrowed money to purchase stock to obtain "power" or control over World T. and I. Corporation I think that the possibility of increased dividends by lending to World T. and I. Corporation must be taken to be too remote to characterize the lending of the borrowed money to it without interest as use for the purpose of earning income from the property represented by the loan. It is the loan itself rather than the shares that I think Rand J. refers to when he says the statute means "the income produced by the exploitation of the property itself".

In my view, however, during the material time the possibility of increased dividends on the shares of World T. and I. Corporation held by the appellant was the only prospect of income even indirectly flowing from the use to which the appellant put the money it had borrowed from Caus Investment and Finance Company Limited. There was, in my view, as I have already said, no arrangement between the appellant and World T. and I. Corporation for sharing the profits or losses of the venture in purchasing the Scotch fillings or was there any other agreement or arrangement in effect pursuant to which remuneration in the form of interest or otherwise was accruing. Nor was interest or any other form of remuneration being received or claimed in the material period and this even though the effect of the loan on the company's affairs was being felt. Understandably nothing appeared in the appellant's financial statements for the years in question to reflect any income right arising from the loan to World T. and I. Corporation. The statement of Mr. Gilmour that if satisfaction had not been obtained through the transfer of the fillings to the appellant more interest than the token payment of $10,000 ultimately made would have been paid is moreover in my view merely speculation. As I see it, throughout the relevant period there was no right to more remuneration or to any remuneration. The $10,000 itself was not earned as interest. It was a lump sum payment, a mere token in amount and neither more nor less in substance than a gift which after the material time top management, on the advice of their tax consultant, required World T. and I. Corporation to pay to the appellant. In my opinion therefore the statutory requirement that the borrowed money be *used for the purpose of earning income from* (the appellant's) *property* was not satisfied.

The appeal on this issue accordingly fails.

I turn now to the foreign exchange loss which the appellant seeks to deduct in computing income for its fiscal period which ended on August 31, 1961. In the course of its business the appellant purchases supplies of Bourbon whiskeys distilled in the United States, barrels, flavourings and other items of a current nature from other Schenley companies in the United States and elsewhere and sells to companies of this group both matured and unmatured liquors which it has produced in Canada. On the account of these transactions maintained by the appellant there was on August 31, 1961 a balance of $3,051,000 admittedly owing to Schenley Industries Inc. in United States funds. It is agreed that this indebtedness had been expressed at par in the appellant's accounts. Some of it had been outstanding for several years, the appellant having purchased some years earlier, on terms not requiring immediate payment, some large quantities of Bourbon fillings for re-distillation and further maturing in Canada before being marketed. At the beginning of the appellant's 1961 fiscal period that is to say on September 1, 1960 the balance owing by the appellant in this account had stood at $2,666,135 United States dollars and at that time and for some years prior thereto the Canadian dollar had been above par in terms of United States dollars. In the course of the 1961 fiscal year of the appellant, however, the value of the Canadian dollar declined and on August 31, 1961 was below par in United States dollars. On that date, as a result of a suggestion by the Canadian income tax authorities that because it had been outstanding for several years some of this indebtedness would not qualify for deduction in computing income until the year in which it was paid the appellant, on the advice of Mr. Gilmour, purchased the required number of United States dollars and paid off almost all of the balance owing in this and several other smaller accounts recording transactions of a current nature. It purchased the United States dollars, however, at a premium of $96,364, which is the item the deductibility of which is now in issue. Most of the funds necessary to purchase the required amount of United States dollars were raised by borrowing $3,100,000 Canadian dollars from Schenley Industries Inc.

Prior to this occasion the appellant had recorded foreign currency transactions on what the witness called a "cash" method. In it, on a sale or purchase of goods for United States dollars, the transaction would be entered at the amount thereof converted at the then prevailing exchange

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rate into Canadian dollars. No account would thereafter be taken of oscillations in the exchange rate until the transaction was completed by actual payment on which date appropriate entries would be made to record any change in the amount of Canadian dollars required to complete the transaction. It was in this context that Mr. Gilmour recommended some time during the 1961 fiscal period, when the suggestion by the Canadian tax authorities with respect to the non-deductibility of items in the merchandising account was made, that the balance in the merchandising account be settled by actual payment at the end of each fiscal period. Such settlement was, however, carried out only on the one occasion as in the 1962 fiscal period the appellant adopted an accrual method which differed from the earlier method in that at the end of the fiscal period the amount necessary to complete outstanding transactions was computed at the exchange rate prevailing on that date and profit or loss taken into income accordingly.

In my opinion the loss here in question was clearly deductible in computing income for the year 1961 not only because it resulted on the purchase of United States funds purchased for the purpose of discharging, and thereafter used to discharge, obligations incurred in trading transactions and thus represented a loss realized in the year in accordance with the accounting method which had been followed in earlier years and was being followed in the year in question but also because it represented a loss which had in fact been sustained on trading account in the year as a result of the decline in the value of the Canadian dollar and which was merely measured and determined by the transaction of August 31, 1961. *Vide Eli Lilly and Company (Canada) Ltd v. M.N.R.*,[2] *Tip Top Tailors Ltd v. M.N.R.*[3] and *Canadian General Electric Co. v. M.N.R.*[4]

Counsel for the Minister did not dispute the loss or the amount of it but made three submissions in support of the Minister's position. It was said first that the evidence showed that the appellant's liability for a large portion of the balance owing in the account had been in existence for more than ten years and that it should on that account be regarded as having been a capital rather than a trading

[2] [1955] S.C.R. 745.
[3] [1957] S.C.R. 703.
[4] [1962] S.C.R. 3.

obligation. With respect to this submission I am unable to see how, in the absence of any applicable statutory provision, the mere length of time in which the obligation was outstanding has any effect in a situation of this kind in changing what was, at the time it was incurred, a trading obligation into an obligation on capital account.

The second point made was that the loss in question was connected with an outlay that was not made for the purpose of gaining or producing income from the appellant's business within the meaning of the exception to section 12(1)(*a*) of the Act. It was said that the loss was incurred simply because the appellant decided to pay the debt when there was no business reason to do so. This submission treats the loss as having been caused by the transaction by which the debt was paid and disregards the fact that the liability to pay some three million United States dollars was incurred in the course of trading and thus was an expense incurred for the purpose of gaining or producing income. While the payment of that obligation, whenever made, would be in itself a transaction in the course of trading, that particular transaction could scarcely be an income producing or earning transaction even though the amount of the expense itself in terms of Canadian dollars might grow or decline as the exchange rate fluctuated. At any particular moment while the obligation was outstanding and the real extent of this obligation was the amount of Canadian funds necessary to purchase enough United States dollars to pay it, and whether or not in the accounting method which the appellant had followed, a profit or loss might, on the payment of the obligation, appear and be taken into income that profit or loss could not arise from the transaction itself. It could only arise from the fluctuation of the exchange rate while the obligation incurred in the course of trading remained outstanding. Whatever the reason for paying the obligation on any particular day the transaction itself, in my opinion, therefore could have no effect whatever in producing an exchange profit or loss but could simply quantify and determine once and for all an exchange profit or loss which had in fact arisen from other causes. In my view by paying the obligation the appellant was able to compute and show more accurately the profit from its business for the year than if the obligation had been left unpaid.

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Finally it was urged that the loss arose from an artificial transaction carried out when payment had not been demanded and solely for tax reasons and on that account as well should not be regarded as having been incurred for the purpose of gaining or producing income from the appellant's business. To my mind this submission is a mere extension of the previous submission and is also unmaintainable. The fact that payment had not been demanded is in my view irrelevant and the argument as a whole disregards the fact that the loss arose not from the transaction carried out on August 31, 1961, which no doubt was carried out for tax reasons, but from decline in the value of the Canadian dollar which made it necessary to use more Canadian dollars to meet, on whatever day payment might be made, an obligation incurred in the course of trading. By paying the account on the day chosen, regardless of the reason for deciding to do so, the appellant, in my view, merely quantified in Canadian dollars the extent of its trading obligation in United States dollars and thus determined once and for all the amount of a loss sustained in the year by not having discharged the obligation before the value of the Canadian dollar declined.

The appeal on this issue accordingly succeeds.

In the result, therefore, the appeal will be allowed to the extent indicated in these reasons. As the appellant has had substantial success it will be entitled to the general costs of the appeal but not including any items pertaining exclusively to the issue on which it has failed. The Minister may tax and set off against the costs so awarded to the appellant any taxable costs he may have incurred pertaining exclusively to the issue on which he has succeeded. On taxation one-third of the time taken for the trial is to be taken as applicable to the issue on which the Minister succeeded and two-thirds of the time to the issues on which the appellant succeeded.

BETWEEN:

KNAPSACK ACTIENGESELL-SCHAFT .... APPLICANT;

Ottawa 1968

Jan. 30

Feb. 1

AND

THE DEPUTY ATTORNEY GENERAL OF CANADA .... RESPONDENT.

Post Office—Patents—Jurisdiction—Postal Services Interruption Relief Act, S. of C. 1967, c. 77—Failure to file patent application within year of foreign application—Waiver of time requirement of Patent Act, s. 29(1).

Held (dubitante), where an interruption of normal postal services in Canada prevents an applicant for a Canadian patent from filing his application until after the expiration of twelve months from the date he filed application for a foreign patent for the same invention a Judge of the Exchequer Court has authority under the *Postal Services Interruption Relief Act,* S. of C. 1967, c 77 (all other conditions thereof being met) to waive the twelve months requirement stipulated by s 29(1) of the *Patent Act* and to fix another time requirement therefor.

APPLICATION.

Donald A. Hill for applicant.

C. R. O. Munro, Q.C. for respondent.

JACKETT P.:—This is an application under the *Postal Services Interruption Act,* chapter 77 of the Statutes of 1967, for an order extending the time within which Canadian Patent Application Serial No. 938,112 should have been filed in order to claim the rights accorded by section 29 of the *Patent Act,* R.S.C. 1952, chapter 203, having regard to Application Serial No. K 53 701 IVb/12o filed August 8, 1964 in Western Germany.

On August 8, 1964, an application was filed under the law of Western Germany for a patent for a certain invention and on August 13, 1965, an application was filed for a patent for the same invention under the *Canadian Patent Act.*

I am satisfied that, had it not been for the interruption in normal Canadian postal services which occurred between July 22 and August 7, 1965, the Canadian application would have been filed prior to August 8, 1965. The result is that section 29(1) of the *Patent Act* (which

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provides that an application for a patent for an invention filed in Canada by a person entitled to treaty protection who has filed an application for the same invention in any one of certain other countries "has the same force and effect" as it would have had if it had been filed in Canada on the earliest date on which the foreign application was filed in the other country "if the application in this country is filed within twelve months" from such earliest date) does not apply to this Canadian application and the applicant is not entitled to the benefit of the date of the foreign application if that should ever turn out to be material.

On March 1, 1967, Royal assent was given to a statute of the Parliament of Canada (chapter 77 of 1967), reading in part as follows:

> 1. This Act may be cited as the *Postal Services Interruption Relief Act.*
>
> 2. Where as a result of the interruption of normal postal services which occurred between the 22nd day of July and the 7th day of August, 1965 or any subsequent interruption of normal postal services in Canada of more than forty-eight hours' duration however caused, a person has suffered loss or hardship by reason of his failure to comply with any time requirement or period of limitation contained in any law of Canada, he may, on fourteen days' notice in writing to the Deputy Attorney General of Canada and to any other person who he has reason to believe may be affected by any order made pursuant to section 3 as a result of an application by him under this section, apply to a judge of the Exchequer Court of Canada for relief.
>
> 3. If the judge to whom an application under section 2 is made is satisfied
>
> (*a*) that the applicant has suffered loss or hardship as a result of any interruption described in that section,
>
> (*b*) that the applicant took such reasonable steps as were open to him to comply with the time requirement or period of limitation without avail, and
>
> (*c*) that the application was made without undue delay,
>
> he may, after affording to any person who may be affected by any order made pursuant to this section as a result of the application an opportunity to be heard on the application or to make representations in connection therewith, and subject to such conditions, if any, as to him seem just,
>
> (*d*) make an order waiving the time requirement or period of limitation in relation to the applicant and fixing such other time requirement or period of limitation in relation thereto as in his opinion the circumstances warrant, and
>
> (*e*) make such further order as, in his opinion, is necessary to permit the applicant effectively to do any thing or exercise any right that he would have been able to do or exercise if he had not failed to comply with the time requirement or

period of limitation, including, where the time requirement or period of limitation with which the applicant failed to comply relates to the commencement or carrying on of any proceeding authorized or provided for under any law of Canada, such order as he considers necessary to enable the proceeding to be commenced and continued or to be carried on as though the applicant had not failed to comply with that time requirement or period of limitation.

As indicated above, I am satisfied that, if it had not been for the interruption in postal service, the Canadian application would have been filed in time to have made section 29(1) applicable to it. I am satisfied that being deprived of whatever advantages that provision confers is a "hardship" within the meaning of the *Postal Services Interruption Relief Act*. I am also satisfied that the applicant took such reasonable steps as were open to it to file its Canadian application within the twelve month period referred to in section 29(1).

There are three matters, however, that I am not satisfied about or concerning which I have difficulty, *viz.*:

(a) There is no material before me to establish that the application that I am considering was made without undue delay. (The applicant may have leave to file such material.)

(b) I have doubts as to whether the twelve month period in section 29(1) of the *Patent Act* is a "time requirement or period of limitation" within the meaning of those words in the *Postal Services Interruption Relief Act*.

(c) I have doubts as to whether section 3 of that Act authorizes the Court to make an order that waives a "time requirement" and substitutes as a "time requirement" a time that has already gone past, which is the type of order that the applicant seeks and, indeed, is the only type of order that will, apparently, give him the relief that he feels that he requires.

To me, the type of case to which the words "time requirement" in the *Postal Services Interruption Relief Act* obviously apply is where a statute authorizes something to be done within a fixed time. Such provisions as a provision authorizing an appeal or a legal proceeding to be launched, but only if it is launched within a fixed time, or

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authorizing an application to be made for something, but only if it is made within a fixed time, are clearly within the statute. Where an interruption in postal services has prevented such a proceeding being launched or such an application being made within the time fixed, the Court might under section 3(*d*) waive the time requirement and fix some other time requirement in relation to the bringing of the proceeding or the making of the application.

This is not such a case. In this case there was no limitation period imposed by the statute in respect of the filing of the application, which has, I understand, been filed and has been dealt with by the Commissioner to the point where a patent may be expected to issue before long. In this case, filing the application within the specified twelve month period is a condition precedent to the operation of the substantive rule contained in section 29(1) of the *Patent Act* in respect of this application (that is, there is, in one sense of the words, a "time requirement" with respect to the applicant having the advantage of the foreign filing date), and the question is whether such a condition precedent to the operation of a substantive rule framed by reference to a period of time is a "time requirement" within the meaning of the *Postal Services Interruption Relief Act*. (It seems clear to me that the English expression "period of limitation" refers to the sort of period established by an act concerning "Limitation of Actions". See, for example, "The Canadian Abridgement".)

The question as to whether the words "time requirement" must be restricted to a "time requirement" for doing something (as opposed to a time element in a condition precedent to the operation of a substantive rule of law) cannot be considered completely divorced from the further question, to which I have already referred, as to the nature of the relief that the Court can order.

In the first place, when one looks at section 3(*d*), one sees that the Court may make an order "waiving the time requirement" and "fixing such other time requirement" as the circumstances warrant. This would seem to point, most directly at any event, to fixing a new "time requirement" so that the applicant can do something following the Court order that he is unable to do without a Court order by reason of the original "time requirement" that operates as a bar.[1] What I am asked to do in this case, however, is to make an order waiving "the time requirement prescribed by section 29(1) ... within which Canadian Patent Application Serial No. 938,112 should have been filed in order to claim the rights accorded by the said Section", and fixing August 14, 1965 (a day that will have preceded the Court's order) as the day "on or before which the said application is to be filed in order to comply with the time requirement of section 29(1)".[2] I have a little difficulty in regarding the fixing of a past day as the day before which something must have been done as the fixing of a "time requirement".

This difficulty is, if anything, underlined when I look at section 3(*e*) by which the Court, having made the order contemplated by section 3(*d*) is authorized, in addition, to make a further order

> "to permit the applicant effectively to do any thing or exercise any right that he would have been able to do or exercise if he had not failed to comply with the time requirement,"...

Certainly, if Parliament had had in mind, when it enacted the *Postal Services Interruption Relief Act,* only the sort of case where a substantive rule was to be allowed to operate notwithstanding failure to comply with a condition precedent containing a time element, one would have expected that the relieving statute would have merely provided generally for a modification of all such conditions precedent accordingly so that the Court having occasion to apply the substantive rule could consider the matter in the light of the particular rule as so modified. In other words there would, I should have thought, have been a general statute which, when applied to section 29(1), would, on proof of the conditions precedent spelled out in the statute, cause the words in section 29(1)—"if the application ... is filed within twelve months"—to read, "if the application ... is filed within twelve months or such extended period as is reasonable having regard to the interruption in postal

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[1] Strictly speaking this would be giving the legislation prospective, not retrospective, force.

[2] To do this, it is necessary to construe the statute as authorizing the Court to make an order with retrospective effect It will give past acts an effect that they did not have when they were done

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service". There would be no need for a special application in such a case. The only reason for a special application such as is contemplated by the Act would appear to be to enable the applicant to do some thing, or exercise some right, that he would otherwise be prevented from doing or exercising.

I recognize, however, that giving the widest possible sense to the language employed, it may have been intended to apply the statute to both classes of case. I realize also that, from a practical point of view, there are advantages in permitting an application in a case such as that raised by section 29(1). I am also apprehensive that a judge acting under this statute is *persona designata* and that there may be no appeal from a refusal to make an order sought under the statute. I propose, therefore, notwithstanding my very considerable doubts, to interpret the statute in the widest possible manner.

In coming to this conclusion, I am conscious that I am construing the statute without the advantage of argument by counsel for a party who may be adversely affected and that such an argument might put the operation of the statute into quite a different perspective. In the circumstances, I think I should indicate that, in the event of being met with such an argument in some other case in the future, I shall not regard myself as bound by this decision.

Upon the applicant filing material that satisfies me as to the requirement in section 3(*c*), I will be prepared to grant an order under the statute which, as it seems to me, might be framed somewhat as follows:

Upon application...

It having been made to appear

(a) that Canadian Patent Application Serial No. 938,112 was filed on August 13, 1965 and, except for the interruption in Canadian postal services which occurred between July 22 and August 7, 1965, would have been filed prior to August 8, 1965;

(b) that the person by whom such application was filed also filed an application under Western German patent law for a patent for the same invention on August 8, 1964;

(c) that the applicant took such reasonable steps as were open to him to comply with the time requirement contained in section 29(1) of the *Patent Act* in relation to the application aforesaid without avail; and

(d) that the application to this Court was made without undue delay;

It is hereby declared that the undersigned judge of the Exchequer Court of Canada is satisfied that the applicant has suffered loss or hardship as a result of the aforesaid interruption of normal postal service;

And it is hereby ordered that the time requirement contained in section 29(1) of the *Patent Act* within which Canadian Patent Application Serial No. 938,112 should have been filed in order that the provision contained in such statutory provision should apply to such application be waived and that the 14th day of August, 1965 be and is hereby fixed as the day on or before which the said application should have been filed in order to comply with the time requirement of the aforesaid section 29(1).

As indicated above, material may be filed on the question of undue delay and the application brought on for further hearing at which time I shall be glad to hear submissions as to the form of the order.

Winnipeg 1967 Dec. 12-13
Ottawa 1968 Feb. 5

BETWEEN:

THE MINISTER OF NATIONAL REVENUE .... APPELLANT;

AND

CLEMENT'S DRUG STORE (BRANDON) LIMITED .... RESPONDENT.

Income tax—Capital cost allowances—Sale of business to employee—Cost of fixtures specified in contract—Whether amount reasonable—Contract bona fide—Income Tax Act, s. 20(6)(g).

A pharmacist employed in a retail drug store contracted to buy his employer's business for $110,000, of which $45,000 was allotted by the contract to fixtures (principally solid oak shelving and beam fixtures installed in 1913), but no amount was allotted to any other assets. The fixtures had originally cost some $8,700 but their undepreciated capital cost at the time of the contract was $962. The contract provided that if the monthly lease of the store premises were terminated

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within nine years or the rent substantially increased the price of the business should be $33,779 (the value of the stock-in-trade) plus 90% of the profits until termination of the lease, but this contingency did not occur. The contract was assumed by respondent company, which carried on business in the premises under a monthly lease for nearly three years when it entered into a long-term lease for enlarged premises and undertook as a term thereof to make certain alterations, in the course of which it substituted new shelving for the oak shelving. In assessing appellant the Minister applied s. 20(6)(*g*) of the *Income Tax Act* and reduced the capital cost of the fixtures from $45,000 to $3,000 as the amount which could reasonably be regarded as the consideration therefor.

Held (affirming the Tax Appeal Board), the assessment could not stand. The rule in s. 20(6)(*g*) did not apply in the circumstances. The decisive circumstance was the actual cost to respondent of the fixtures which was $45,000, that being the amount actually paid under a *bona fide* contract negotiated at arm's length.

INCOME TAX APPEAL.

F. L. Dubrule and *J. Halley* for appellant.

Frank O. Meighen, Q.C. for respondent.

CATTANACH J.:—This is an appeal by the Minister from a decision of the Tax Appeal Board[1] dated April 22, 1966 in respect to the Minister's assessment to income tax for the respondent's 1960 and 1961 taxation years. By the assessments in question the Minister reduced the capital cost allowance claimed by the respondent in respect of furniture, fixtures and equipment purchased by it from $45,000 to $3,000 and computed the tax payable accordingly.

The transaction which gave rise to this appeal was the sale in 1959 of a retail drug business carried on in the City of Brandon, Manitoba. This business was begun originally by D. E. Clement, a member of the Clement family, in 1913 in a building known as the Clement Block, a five storey building situated in the centre of the downtown area of the city. The four upper storeys contained offices and the street level floor housed a variety of businesses over the years but including the drug store throughout those years. The building was owned by a number of the members of the Clement family of which Mr. D. E. Clement was one.

[1] (1966) 41 Tax A.B.C. 125.

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In 1934 Clement's Drug Store Limited was incorporated to acquire and carry on the drug store on the identical site. At that time Mr. W. P. Lowres, who had been associated in partnership with Mr. D. E. Clement prior thereto, acquired a substantial share interest in the Company and eventually, in or about 1948, he became the beneficial owner of all issued and outstanding shares in the Company.

The business carried on throughout the years can best be described as a reputable family pharmacy. While a variety of items normally associated with a drug store were sold, nevertheless, much emphasis was placed upon the expert and accurate filling of prescriptions. The fixtures, the greater portion of which consisted of solid oak shelving and beam fittings, were custom built and installed in 1913 and were in continuous use since that time. They were designed to complement and accentuate the high repute and substantial nature of the pharmacy business to be carried on in the premises. Representations of the mortar and pestle were carved into the oak fixtures to complete the motif and coloured apothecary globes were displayed.

When the fixtures were acquired by Clement's Drug Store Limited in 1934 they were taken into the Company's opening balance sheet at $4,000. Mr. Lowres testified that this was during the depression years when the value of all assets was extremely low. Between 1935 and 1938 there were additions to the fixtures in the amount of $3,042.59 making a total of $7,042.59 the undepreciated capital cost of which was $814.58 as at December 31, 1948. Between 1949 and 1959 further additions were made in the amount of $1,648.76 thereby bringing the total cost of these assets to the Company to $8,691.35, the undepreciated capital cost of which was $962.54 as at December 31, 1959. However, Mr. Lowres said that in the depression years of the thirties many items were claimed as expenses in the year of purchase and not depreciated.

The retail drug business carried on first by Mr. D. E. Clement and then by his successor, the Company owned by Mr. Lowres, was particularly successful and over the years became increasingly more successful. In the Rexall method of drug merchandising this store always stood in the top listings based upon the value of purchases from Rexall.

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Mr. Lowres employed a number of qualified pharmacists. In 1957 he employed John Garth Allen in that capacity on a salary and bonus basis. Mr. Allen was anxious to engage in the drug business on his own account. Some time in 1958 he indicated to Mr. Lowres that he wished to purchase the business to which overture Mr. Lowres was not unduly receptive. Mr. Allen, therefore, investigated the possibility of purchasing two or three other businesses. However Mr. Allen, who was young and ambitious, persisted in his efforts to purchase the business owned by Mr. Lowres with which his employment had made him familiar.

In 1959 Mr. Lowres agreed to sell the business for a price of $100,000.

Accordingly an agreement between Clement's Drug Store Limited as vendor, John Garth Allen as purchaser and William Percy Lowres as convenanter, was entered into on December 30, 1959 whereby the business was sold to the purchaser, Mr. Allen, for $100,000 made up of fixtures at $45,000 and stock-in-trade to be determined and valued as at December 31, 1959. The stock-in-trade was subsequently determined to have been $33,779.23 as at that date.

The purchase price was payable, $20,000 in cash and the balance by equal consecutive annual payments of $8,000 payable at $4,000 on the last day of June and December commencing on the last day of June, 1960.

Interest was payable on the outstanding balance at 3 per cent beginning January 1, 1963 until January 1, 1965 when the interest on the outstanding balance of the purchase price would be at the rate of 4 per cent.

Mr. Allen undertook to employ Mr. Lowres as a business consultant and adviser for a period of ten years or so long as Mr. Lowres or his wife should retain ownership of at least 51 per cent of the shares of the vendor company, whichever should be the earlier date at an annual salary of $4,800 payable monthly.

By the agreement dated December 30, 1959 it was provided by paragraphs 10 and 11 thereof that upon the incorporation of a new company by Mr. Allen that a new agreement substantially embodying the terms of the agreement dated December 30, 1959 would be entered into by the parties and the new company would then, in effect, stand in the place of the original purchaser, Mr. Allen.

A new company was incorporated, which is the present respondent, and an agreement was made dated December 23, 1960 to which the respondent was also a party whereby it acquired the business and assets of the drug store and undertook obligations substantially similar to those in the prior agreement.

The present appeal was heard and argued on the assumption that the respondent herein should be regarded as the original purchaser. A contrary assumption would not have a material bearing on the eventual outcome of the present appeal. If the original purchaser were Mr. Allen personally, and not as agent or trustee for the company to be formed, the respondent would be deemed to have acquired depreciable property at the same capital cost as the capital cost to Mr. Allen (see section 20(4) of the *Income Tax Act*) since any transaction between Mr. Allen and the respondent, which he controlled, would not be at arm's length (see section 139(5) and 139(5a)).

At no time during the conduct of the drug store business did the proprietor have a long term written lease with the landlord. Presumably when Mr. D. E. Clement was the owner of the drug store there was no necessity for a long term lease because he was a co-owner and closely related to the other co-owners of the building and I would presume that similar considerations prevailed when Mr. Lowres first became associated with Mr. Clement in the business. In all likelihood these considerations may have continued when Mr. Lowres acquired the controlling interest of the Company which became the owner of the drug store. The premises were let on a monthly basis and the oral monthly lease could have been terminated on one month's notice, a circumstance which was well known to all parties to the sale of the business.

I have no doubt that the location of the business was one of the paramount considerations present to Mr. Allen's mind when he was negotiating for its purchase. Accordingly the agreements contained a provision covering the contingency that the landlord might terminate the lease.

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Paragraphs 3 and 4 of the agreement dated December 23, 1960 read as follows:

3. The Purchaser will employ the Vendor as a business consultant and adviser for a period of ten (10) years or so long as the Party of the Fourth Part or his wife shall retain the ownership of at least fifty-one (51%) per cent of the capital stock of the Vendor whichever shall be the earlier date or for such lesser period as the Purchaser may have to assume by reason of the fact that it is no longer able to occupy the premises presently occupied by the Vendor by reason of the refusal of the owners thereof to permit the continued occupancy thereof by the Purchaser either through refusal to continue the rental arrangement presently in existence, by the giving of notice by the Landlord or by the Landlord requiring the Purchaser to pay a rental in excess of Eight Thousand ($8,000 00) Dollars per annum and the Purchaser being unable to obtain substitute business accommodation in the City of Brandon in order to continue the operation of said business. The salary to be paid to the Vendor shall be Forty-eight Hundred ($4,800 00) Dollars per year. If prior to the thirty-first day of December, A.D. 1969 the lease or rental arrangement with respect to the premises to be occupied by the Purchaser shall be terminated as aforesaid or should the Landlord require a rental to be paid in excess of the sum of Eight Thousand ($8,000 00) Dollars per year and the property be surrendered accordingly and the Purchaser shall not be able to acquire suitable premises in the City of Brandon to carry on the said business but shall be desirous of acquiring other premises which it considers will not be so suitable then the salary to be paid hereunder shall be the subject of arbitration. The Purchaser shall appoint one arbitrator, the Vendor another and the two arbitrators so chosen shall choose a third and their decision as to the salary to be paid thereafter shall be final and binding upon the parties hereto.

4 If prior to the thirty-first day of December, A.D. 1969 the lease or rental arrangement with respect to the premises to be occupied by the Purchaser shall be terminated by the Landlord or should the Landlord require a rental to be paid in excess of the sum of Eight Thousand ($8,000 00) Dollars per year and the property be surrendered accordingly and should the Purchaser be unable to obtain other suitable business premises in the City of Brandon to carry on said business the purchase price shall subject to the provisions of this paragraph be reduced on the basis hereinafter set forth, namely:

> The value of the stock and fixtures as determined as of the thirty-first day of December, A D. 1959 in the sum of Thirty-three Thousand Seven Hundred and Seventy-nine Dollars Twenty-three Cents ($33,779 23) and there shall be added thereto ninety (90%) per cent of the profit of the business each year thereafter (after payment of income tax) up to the aforesaid termination of the lease and the Purchaser shall pay unto the Vendor the total amount thereof not to exceed in any event One Hundred Thousand ($100,000.00) Dollars and any payments made hereunder shall be applied thereon. In the event that the termination of the lease should take place in mid-year then the pro-rata portion of the profit for such year shall be determined on the profit of the preceding year. Should the Purchaser find other business premises in the City of Brandon which it considers will not be suitable for

> the carrying on of the said business and should it leave the present premises then the Purchaser may require the balance of the purchase price to be set by arbitration in which case the Purchaser shall choose one arbitrator, the Vendor shall choose one arbitrator and the two arbitrators so chosen shall choose a third and the decision of the majority of the arbitrators so chosen shall be final and binding upon the parties hereto.

The corresponding provisions of the agreement dated December 30, 1959 are contained in paragraphs 4 and 5 of that agreement except that in paragraph 5 the value of the stock and fixtures as shown in the books of the vendor as at December 31, 1959 is to be taken whereas in the second agreement the value of the stock and fixtures is stated in the specific sum of $33,779.23 which sum is the value of the merchandise inventory as at December 31, 1959 determined shortly after that date.

However the contingency contemplated by the foregoing provisions did not arise.

The respondent continued the business in the same premises held under a monthly tenancy for a period of two years and nine months.

Sometime in the late summer of 1962 a rumour came to the attention of Mr. Allen while he was on vacation that the landlord was negotiating for a lease to a chartered bank for the entire ground floor area of the Clement Block. Such negotiations had been in progress in fact but had broken down, of which circumstance Mr. Allen was unaware and the landlord did not communicate it to him. He therefore cut short his vacation and returned to negotiate a lease for the premises occupied by the drug store. At that time on the ground floor there was a small area occupied by a clothier adjacent to the drug store premises and on the other side of the clothier were premises occupied by a travel agency operated by D. W. Clement who was one of the co-owners of the building. The landlord had experienced difficulty in obtaining satisfactory tenants for the space occupied by the clothier because of the small area. The landlord considered that it would be more advantageous to eliminate that space by dividing it and adding to the areas occupied by the drug store and travel agency. This addition of space was a condition precedent to the landlord entering into a long term lease with Mr. Allen who felt impelled to comply.

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Accordingly a lease dated September 30, 1962 was entered into between the landlord and the respondent covering the increased area for a period of seven years at a monthly rental of $550. By a memorandum annexed to and forming part of the lease, the landlord undertook the necessary construction work to expand the premises, but the respondent undertook to install a new store front to the expanded area of the drug store. The installation of a new store front had been casually broached to Mr. Lowres by the landlord but was never a matter of serious consideration between them. There was no evidence that the possibility of the landlord requiring a new store front to be installed had ever been brought to Mr. Allen's attention.

Mr. Allen investigated the feasibility of matching the oak fixtures already in use in the acquired area but found the cost to be prohibitive. Accordingly he removed the original oak fixtures and installed modern metal fixtures throughout the store. Nothing was realized upon the discarded oak fixtures because they had been custom built for the premises where used and were useless elsewhere. An attempt to realize scrap value was unsuccessful.

Under the terms of the original agreements for sale the balance of the purchase price was to be secured by a chattel mortgage. However, it was not until February 15, 1963 that this requirement was complied with by two instruments bearing that date covering the fixtures and stock-in-trade used in the business securing the then outstanding amount of $68,000 and subject to a prior chattel mortgage in favour of the respondent's bank.

Mr. Allen testified that when he purchased the fixtures he had no intention of replacing them and that his decision to do so was necessitated by the circumstances outlined above. He added that they were more than satisfactory for the purpose of conducting a retail drug store. As an indication of the efficiency of the fixtures it was established that the business under Mr. Allen's management increased its Rexall rating to first and second in 1961 and 1960 respectively. Rather than becoming obsolete the fixtures had become enhanced in value.

He also testified that certain of the equipment originally purchased was still in use, a schedule of which was filed in evidence as Exhibit 11. Mr. Allen assigned values to each such item totalling $12,170. No consistent method of evaluation was adopted. In some instances cost was used, in others replacement value and in some instances a depreciated value was used, but in any event I am certain that Mr. Allen's estimate of $12,170 represents a value very approximate to the value of those items still in use. In addition he had also purchased an outside neon sign which he valued at $1,500.

Mr. Lowres gave evidence to like effect as to the efficiency of the fixtures and further testified that he would not have sold them for less than $45,000. In fixing a price of $100,000 in response to Mr. Allen's desire to purchase the business he said that such was the worth of the business to him. I should add that subsequent to the agreement dated December 30, 1959 Mr. Lowres deposited $10,000 in the vendor company's current bank account. This account was purchased and transferred to the respondent. Mr. Lowres said that he did this to facilitate Mr. Allen carrying on the business and that it was in the nature of a loan. By paragraph 15 of the agreement dated December 23, 1960 the amount of $10,000 was added to the purchase price. I should also add that by the two agreements the respondent assumed all trade liabilities of the vendor as at December 31, 1959 which totalled $18,275.

I would add that in preparing his tax return Mr. Lowres reported the sale of the fixtures and equipment at $45,000 and brought into income capital cost allowance recaptured in the amount of $1,650.80.

The amount of $45,000 as the price of the fixtures and equipment as recited in both of the two agreements for sale dated December 30, 1959 and December 23, 1960 was arrived at by negotiation between Mr. Lowres and Mr. Allen. An evaluator was not engaged to fix prices on the assets, but the amount was settled upon by the vendor and purchaser.

The value of the total assets sold was $128,275 consisting of current assets such as cash on hand, bank account, accounts receivable, merchandise inventory and prepaid expenses, to the total amount of $45,844.02, investments in the total amount of $1,055 fixed assets at $45,000 making a total of tangible assets of $91,899.02 added to which was goodwill at $36,375.98. When the total of liabilities

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assumed in the amount of $18,275 is deducted from the total of the assets acquired being in the amount of $128,-275, the net sale price is $110,000. The only figures in dispute between the parties is the $45,000 attributed to fixtures and equipment by the respondent and an amount of $36,375.98 to goodwill.

The Minister says that an amount of $3,000 only can reasonably be attributed to the consideration for the fixtures and equipment from which it follows that an amount of $78,375.98 would be attributed by the Minister to goodwill, an increase of $42,000 over the amount of $36,375.98 attributed to goodwill by the respondent.

The issue between the parties, therefore, resolved itself into the problem of determining on the facts as disclosed by the evidence, what part of the total purchase price can reasonably be regarded as having been the consideration for the depreciable property purchased, i.e. the fixtures and equipment.

The statutory provision under which the matter arises reads as follows:

> 20. (6) For the purpose of this section and regulations made under paragraph (*a*) of subsection (1) of section 11, the following rules apply:
>
> . . .
>
> (*g*) where an amount can reasonably be regarded as being in part the consideration for disposition of depreciable property of a taxpayer of a prescribed class and as being in part consideration for something else, the part of the amount that can reasonably be regarded as being the consideration for such disposition shall be deemed to be the proceeds of disposition of depreciable property of that class irrespective of the form or legal effect of the contract or agreement; and the person to whom the depreciable property was disposed of shall be deemed to have acquired the property at a capital cost to him equal to the same part of that amount;
>
> . . .

The argument of counsel for the respondent, as I understood it, was that the sale was an arm's length transaction between two knowledgeable persons both of whom were completely familiar with the business and knew its potentialities and who also knew the value of the fixtures as they were. He also pointed out that although the oak fixtures custom built for the premises were replaced by modern metal ones within twenty-one months of the purchase, this was done only for the reason that to obtain a long term lease the respondent was obliged to rent a larger area. He emphasized that although the greater bulk of the oak fixtures had to be discarded, nevertheless, some of the equipment which had been purchased was still being used in the renovated premises which equipment had a conservatively estimated value of $12,170. This fact, he contended, leads to an irrefutable conclusion that the amount of $3,000 attributed by the Minister as consideration for the purchase of the depreciable property is not reasonable and that the true consideration for the depreciable assets was the price of $45,000 arrived at by the parties to the sale thereof.

The assessments carry a statutory presumption of validity and stand until they have been shown to be erroneous either in fact or in law. Therefore, to succeed in this appeal the respondent must prove that the finding of the Minister that the capital cost to the respondent of the depreciable assets in question was $3,000 was erroneous. (*Vide Johnston v. M.N.R.* [1948] S.C.R. 486 at 489).

I am completely satisfied on the evidence that the assets were not inefficient, obsolete or in need of replacement at the time of their purchase. On the contrary I am satisfied that the respondent would have continued to use them for a long period of years and that the decision to replace those fixtures with modern metal ones was dictated by the respondent's desire for a long term lease of the premises which the landlord would not give unless an enlarged area was covered by such a lease.

The crux of the argument put forward by counsel for the Minister was, as I understood it, that, assuming the statutory rule outlined in section 20(6)(*g*) of the *Income Tax Act* applies, the question is then, what amount can reasonably be regarded as having been consideration for the depreciable property. He contended that an amount of $3,000 is the amount which can be reasonably so regarded, upon which assumption the Minister based his assessments and that the balance of the purchase price, after deducting the value of the inventory purchased, can be reasonably regarded as being in consideration of something else, i.e. goodwill.

In support of the foregoing submission he pointed out that the overall price was to be $100,000, later increased to

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$110,000, and that the only item for which a specific allocation was made in the agreements for sale was that of fixtures and equipment where $45,000 was specified as the price. He added that the delay of the vendor in obtaining a chattel mortgage on the fixtures and stock-in-trade in accordance with the agreement for sale to secure payment of the purchase price of the business was indicative of an overvaluation of the fixtures and equipment. I think this circumstance is equally susceptible of the interpretation that the vendor was satisfied with the integrity of the respondent and its ability to pay from the proceeds of the business in which he acted as a consultant and that resort to this additional security was had when a prior chattel mortgage was placed on the stock-in-trade and new fixtures to secure the respondent's bank loan. Therefore, I do not consider this circumstance to be conclusive either way. His principal submission is, however, that no price was in fact fixed as the purchase price of the drug business at the date of the sale, December 30, 1959, which is the material date, and that it was only when the respondent entered into a lease with its landlord on September 30, 1962 that the price of $110,000 became fixed and determined.

Under the provisions of paragraph 1 and paragraph 15 of the agreement dated December 23, 1960 the purchase price was stated to be $110,000 subject to the assumption by the respondent of accounts payable as at December 30, 1959. Since the tenancy of the premises was a monthly one, provision was made in paragraph 4 of the aforesaid agreement, that in the event of the landlord terminating the monthly tenancy, or exacting a rental in excess of $8,000 per year and the respondent could not obtain suitable premises elsewhere in the city, then the purchase price would be reduced to a value of $33,779.23 for the stock and fixtures plus 90% of the yearly profits of the business to the termination of the lease. Provision was made for a *pro rata* determination of profits if the lease were terminated in mid-year and for arbitration of the purchase price if the respondent carried on the business in premises it considered unsuitable.

Counsel for the Minister contended that the respondent did not obligate itself to pay a purchase price of $110,000 but rather that the minimum amount that the respondent bound itself to pay was the consideration set out in paragraph 5 of the agreement dated December 30, 1959 and paragraph 4 of the agreement dated December 23, 1960. On the assumption that the landlords gave the respondent notice to quit on December 31, 1959, as they were entitled to do and that the respondent would be required to vacate on January 31, 1960, he then computed, by an application of the formula outlined in the foregoing paragraphs of the agreements, the minimum amount which the respondent obligated itself to pay to be approximately $35,000. On that basis he contended that a consideration of $3,000 for the purchase of the depreciable property is a most reasonable proportion bearing in mind that $33,779.23 was the determined value of the merchandise inventory and that the amount of $45,000 attributed by the contract as the consideration therefor is unreasonable.

I am unable to accede to the Minister's contention in this respect. The question is not whether the respondent absolutely bound itself to pay $110,000 for the business, but whether it paid that amount for the business in accordance with the terms of the contract. While it is true that the parties took account of, and provided for, the contingency of the respondent being dispossessed, nevertheless, that contingency did not arise.

Under section 11(1)(*a*) of the *Income Tax Act* it is provided that certain "amounts may be deducted in computing the income tax of a taxpayer in a taxation year" including "such amount in respect of the capital cost to the taxpayer of property, if any, as is allowed by regulation". Section 1100(1)(*a*) by the regulations enacted under section 11(1)(*a*) of the Act provides for deductions for each taxation year equal to the rates specified in paragraph (*a*) applicable to an amount remaining after deducting the amount determined under section 1107 of the regulations, from the undepreciated "capital cost" to the taxpayer. The amount so to be deducted under section 1107, as applicable to the 1954 and subsequent taxation years to the 1966 taxation year, is an amount equal to (*a*) the capital cost of the property that was acquired, (*b*) minus the proceeds of disposition of that property.

It is, therefore, clear that the capital cost allowance is computed upon the actual "cost" of the depreciable assets to the taxpayer for which reason it is incumbent upon me to determine that cost.

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In my view the cost of the depreciable property here in question is $45,000 as determined by the contract among the parties to the sale thereof. That is the amount, under the terms of the contract, the respondent paid for the fixtures and equipment in question. The contract was the subject of arm's length negotiations over a protracted period and was not a mere sham or subterfuge but represents the bargain arrived at by the parties and in my opinion is decisive in the circumstances of this case.

The statutory rule outlined in section 20(6) of the *Income Tax Act* quoted above applies only "where an amount can reasonably be regarded as being in part consideration for disposition of depreciable property of a taxpayer of a prescribed class and as being in part consideration for something else". No question therefore arises under that provision as the circumstances of this particular appeal do not fall within the ambit of the provision.

I do not accept the original premise of counsel for the Minister that the rule so outlined applies here for the simple reason that the parties to the sale of the depreciable property agreed on the capital cost thereof to the respondent, the purchaser.

The appeal is, therefore, dismissed with costs.

Vancouver 1968 Feb. 7-9 — Feb. 21

BETWEEN:

TERMINAL DOCK AND WAREHOUSE COMPANY LIMITED.. APPELLANT;

AND

THE MINISTER OF NATIONAL REVENUE .... RESPONDENT.

Income tax—Subsidiary selling parent's shares to group employees—Contracts for purchase of shares sold to bank at discount—Whether discount deductible—Whether subsidiary in finance business—Income Tax Act, s. 85E(1).

Under a scheme to permit a company's shares to be purchased by its employees and the employees of its subsidiaries, of which appellant was one, appellant (a wharfage company) purchased shares of the parent company at market price and sold them at that price to employees of the parent company and its various subsidiaries over a period of years on certain terms which included an option by the parent company to re-purchase the shares and the payment of interest by the purchasers at 2½% per annum on the balance owing each year.

In 1963, when the amount owing by purchasers of shares was $4,680,631, appellant (which was about to become a public company) sold the purchase agreements to a bank at a discount from their face amount to ensure that the bank would receive interest at 5% per annum on the amount paid. Appellant company sought to deduct the amount of the discount, $292,811, in computing its income.

Held, the amount of the discount was a capital loss and not deductible by appellant.

1. The shares were capital, the relationship between appellant and the employee-purchasers being that of vendor and purchaser and not that of lender and borrower. *Frankel Corp. Ltd. v. M.N.R.* [1959] C.T.C. 244; *Ted Davy Finance Co. v. M.N.R.* [1965] 1 Ex. C.R. 20, referred to.

2. Appellant did not carry on a finance business with respect to the shares since its transactions with respect to them were not for the purpose of gain even though interest was payable on the balance outstanding under the purchase agreements. Hence s. 85E(1) did not apply to enable appellant to treat its agreements with employee-purchasers as inventory of a finance business. Moreover, s. 85E(1) does not permit deduction of a loss sustained on sale of inventory. *Smith v. Anderson* (1880) 15 Ch.D. 247; *Samson v. M.N.R.* [1943] Ex. C.R. 17, referred to; *Irrigation Industries Ltd. v. M.N.R.* [1962] S.C.R. 346; *M.N.R. v. Taylor* [1956-60] Ex. C.R. 3; *M.N.R. v. Curlett* [1967] S.C.R. 280, distinguished.

INCOME TAX APPEAL.

J. G. Alley and *P. N. Thorsteinsson* for appellant.

D. G. H. Bowman and *G. V. Anderson* for respondent.

SHEPPARD D.J.:—In this appeal the appellant contends that the discount charged by a bank in 1963 on the appellant's assignment of certain receivables should be allowed as a deduction from income under sections 85E(1) and 139(1)(*w*) of the *Income Tax Act,* R.S.C. 1952, c. 148 and amendments; on the other hand, the Minister contends that the discount is a loss of capital and not deductible from the taxable income. That is the issue. The facts follow.

The International Milling Company (IMC) of Minneapolis, Minnesota, one of the United States of America, and founded about 1880 as a private company with the objects of milling flour and manufacturing formula feed, has had as subsidiaries Robin Hood Mills Ltd. which (Robin Hood) has, as a subsidiary, the appellant, a British Columbia company incorporated by memorandum. IMC has had also as subsidiaries a Montreal company and a Venezuela company.

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IMC was founded and controlled by Mr. Bean who died about 1930 and was succeeded by his two sons, Francis A. Bean and Atherton Bean, and later by a grandson, John Boynton Bean, one of whom has been president of IMC and of the appellant at all material times. About 1920 the founder decided to admit selected employees of IMC or of one of the subsidiaries, as shareholders of IMC, and that selection was carried out as follows.

The executive committee of IMC would request the executive committees of the subsidiary companies to submit the names of employees who should become shareholders and from that list the executive committee at Minneapolis would approve certain employees and from that approved list the selected employees were ultimately chosen by one of the Bean family. Then the agreements would be entered into.

Exhibit A-3 contains typical examples of agreements outstanding in 1963, namely, No. 589 dated the 26th May, 1947, succeeded by 29th March, 1956; No. 657 of the 4th August, 1948 succeeded by 29th March, 1956; and No. 732 of the 28th September, 1949 succeeded by 29th March, 1956. Each agreement provides for the purchase from the appellant of shares of IMC, the payment by installments over 15 years with interest of $4\frac{1}{2}\%$, or $2\frac{1}{2}\%$ if dividends up to 65% were applied in payment, the pledge of the shares as security and an option back to the vendor.

As business grew and employees increased in number, Robin Hood Mills Ltd. was used to purchase the shares and resell to the employees selected, and later the appellant was substituted for Robin Hood.

By agreement of the 3rd January, 1938 (Ex. R-5) Robin Hood assigned to the appellant all the outstanding agreements to purchase shares and the sums to be paid thereunder subject to the option of repurchase to the Bean family. That substitution made the appellant liable potentially over to Bean for $315,000 which grew in amount to $345,000. That liability arose in that under the respective agreements with the employees the appellant had an option to repurchase the shares at the book value whereas Bean or a foundation held an option over the appellant to repurchase such shares at a fixed price which was less than the book value and resulted in a potential liability of the appellant for the difference.

By agreement of the 24th January, 1938 (Ex. R-6) between the appellant and Francis A. Bean, that potential liability was to be written off over a period of 12 years and by agreement of the 20th August, 1948 (Ex. R-4) the price to Francis A. Bean for his option to repurchase from the appellant was made the equivalent of the appellant's option to purchase from the shareholders.

The parties proceeded in that manner until 1963 and in each year the executive committee at Minneapolis would have the executive committee of the various subsidiary companies select employees as candidates to be shareholders of IMC and these were reviewed by the executive committee of IMC with final selection by one of the Bean family. A day for completion was then fixed and the price of the shares was taken at the book value of the shares on that day. The appellant was notified of such date, the number of the employees purchasing and the amount of the money which the appellant would need to pay for the shares to be and also under successive options from the employee shareholders drawn and signed, and which agreements would ultimately be signed and sealed at Vancouver by the appellant. The appellant would purchase and pay IMC for the shares, the shares would be issued to each employee selected and each employee shareholder would assign and send the share certificate to Minneapolis pursuant to his agreement to give security thereon to the appellant by pledge for the amount payable including interest. The keeping of the share certificates at Minneapolis was merely a matter of convenience. Throughout the same Bean who was president of IMC was also president of the appellant, and also under successive options from the employee shareholder to the appellant and from the appellant to Bean or a foundation, the ownership of the share could revert to the Bean family or a foundation on the shareholder ceasing to be an employee.

The money required by the appellant to purchase such shares was obtained by the appellant selling its own shares to the extent of $2,700,000 and any additional funds required were borrowed from IMC as appears in Exhibit A-6. When a dividend was declared by IMC each employee shareholder was asked to sign a Dividend Disposition Order (Ex. R-1) and if he applied at least 65% of the

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dividend in payment of his purchased shares and interest he was charged $2\frac{1}{2}\%$ for that year on the outstanding balance, otherwise $4\frac{1}{2}\%$.

In 1956 the time for payment by the individual shareholders was extended for 15 years as it was found that by reason of the income tax, some employee shareholders had difficulty in paying the shares within the original 15 years.

In 1963 IMC decided to become a public company, and it was thought preferable not to have the indebtedness of the employee shareholders shown as an asset of the company, as it must appear in a consolidated balance sheet. There was then outstanding, as owing by the employee shareholders, the sum of $4,680,631.60 (Ex. A-2) contained in 819 agreements between the appellant and 355 employees of which employees, 234 were in the United States of America, 108 in Canada, and 13 employees of the Venezuela company. At the time of the discount agreement with the Bank (8th July, 1963, Ex. R-8) the appellant had only two employees with outstanding agreements and the remainder were employees of other companies, either of IMC or of another subsidiary. Thereupon it was decided to sell the agreements between the appellant and the employee shareholders to the First National Bank of Minneapolis, and that was eventually done pursuant to agreement dated 8th July, 1963 (Ex. R-8).

As the agreements by the employee shareholders provided for interest at $2\frac{1}{2}\%$ (with the possibility of $4\frac{1}{2}\%$) the Bank demanded such deduction from the nominal amount owing as would permit it to receive 5% on the price paid. That was eventually agreed to. That discount (being $794,377.80 U.S. funds) with certain offsets, admitted by the appellant, resulted in a net loss of $292,811.40 (Canadian funds) (Ex. A-2).

The appellant contends that the transactions with the employee shareholders were a finance business carried on by the appellant in which business the agreements with the employee shareholders were receivables and inventory, within section 85E(1) as extended by section 139(1)(*w*), therefore there was a loss which should be deducted from the income. On the other hand, the Minister contends that such discount allowed the Bank was a capital loss and not within sections 85E(1) or 139(1)(*w*), and being a capital loss was not to be deducted from income.

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The appellant contends as follows:

2. In the years 1963 and prior the Appellant carried on two businesses, being those of wharf operators in the City of Vancouver and the operation of what was referred to in evidence as "the participation business".

3. The latter business consisted of financing the purchase of International Milling Company stock by employees of International Milling Company, Robin Hood and subsidiaries of Robin Hood including the Appellant itself. The financing was effected by the Appellant acquiring blocks of International Milling Company stock from that company for cash and re-selling to the employees on credit terms.

4. The shares were re-sold to employees at the same price as that at which the Appellant had purchased them but while the Appellant paid cash in buying the shares from International Milling Company, it re-sold to the employees on contracts providing for payment of the price by them over a period of fifteen years with interest on the unpaid balance at 2½%. The employee assigned his stock to the Appellant as security for his debt obligation and commonly applied a percentage of the dividends he received on his stock on account of the principal and interest of his debt obligation to the Appellant. The Appellant had at all times until five years after termination of employment the right to re-acquire the shares from the employee upon payment of a formula price the result of which was that any growth in the equity value of the shares during the time it was owned by the employee accrued to him.

* * *

6. The business of financing the share purchases as above described required the Appellant to be regarded as a money lender engaged in such business of financing. Its business in this regard was essentially that of a finance company, analogous to the common form of business carried on by companies engaged in financing purchases of consumer durable goods such as automobiles, appliances and furniture.

To come within section 85E(1) the appellant must prove, amongst other things, "a business" and that the agreements sold to the Bank were "the property included in the inventory of the business". The appellant concedes the shares in the agreements between the appellant and the employee shareholders were capital, that is, the appellant was not in the business of dealing in shares. The business of a dealer in shares, such as that of a broker, may be *ultra vires* of the memorandum (Ex. A-1) of the appellant, leading to those results in *Sinclair v. Brougham*[1]. However that may be, as the shares were capital, then it is difficult to see how the proceeds thereof, the purchase monies, could be other than capital: *Frankel Corporation Limited v. M.N.R.*[2], *Ted Davy Finance Co. Limited v.*

[1] [1914] A.C. 398. [2] [1959] C.T.C. 244.

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M.N.R.[3]. That difficulty the appellant seeks to avoid by contending that the relation between the appellant and each employee shareholder was exclusively that of lender and borrower and not that of vendor and purchaser. That contention is not made good.

The agreement No. 732 of 28th september, 1949 (Ex. A-3) is a typical agreement and refers to the appellant as "Vendor" and the other party as "Employee" and reads: "WITNESSETH: 1. Shares Sold by This Agreement. The Vendor hereby sells to the Employee 400 shares of the common capital stock of International Milling Company", etc., "2. Purchase Price—Payments of Principal and Interest. the Employee hereby purchases said shares subject to the reservations and conditions as herein set forth and agrees to pay the Vendor therefor the sum of $10,485.40", etc. "4. Collateral Security. The Employee shall keep pledged to the Vendor and in the Vendor's possession to secure the payment of any unpaid balance of the purchase price and interest", etc. "7. Vendor's Options to Purchase Stock." which provides in substance an option to the Vendor to repurchase within 5 years of the Employee ceasing to be an Employee.

A similar relation is indicated by the agreement of 29th March, 1956 (Ex. A-3) which extends the time for payment for an additional 15 years.

It therefore follows that the typical agreements indicate that the transaction between the appellant and the employee's that of vendor and purchaser.

In contrast thereto the appellant contends that it was carrying on a financing business, the equivalent of an automobile finance company. In such instances there are two contracts, one between the purchaser and the dealer which provides for payment by the purchaser and a reservation of title to the dealer as security for payment (a conditional purchase), and the second, the assignment by the dealer of the monies payable and the property reserved as security to the automobile finance company, generally with a guarantee by the dealer. The appellant also contends that it carried on a financing business like the loans

[3] [1965] 1 Ex. C.R. 20; [1964] C.T.C 194

by a household finance company but there the individual borrows on the security of a chattel mortgage on his own property.

Here the relationship between the appellant and the employee shareholders is indicated to be that of vendor and purchaser.

(1) The agreements in question (Ex. A-3) declare:—

(a) that the relationship between the appellant and each employee shareholder is that of vendor and purchaser. The agreements do not refer to them as lender and borrower;

(b) that the debt arises by reason of the purchase price of the shares purchased, hence the relationship is not declared that of lender and borrower nor is the debt declared to arise from a loan.

(2) The agreements in question contain an option to the appellant to repurchase the shares in the event of the employee shareholder ceasing to be an employee. That option can be explained in the sale of the shares to the employee as an attempt to keep the shares in the hands of employees only, but no form of security for a loan commonly provides that upon the borrower repaying the loan and interest, the lender will have an option of repurchasing the subject-matter of the security.

(3) The agreements provide for the appellant having a pledge as security for the purchase price of the shares. That is not the form of security by the financing businesses referred to by the appellant. A pledge may be the common security for a pawnbroker, but it is not argued that the appellant was in business as a pawnbroker nor is that tenable.

On the appellant's contention the appellant was carrying on two businesses, namely, (1) that of a dock and wharfage company and (2) the financing business, but the alleged financing was not a business and hence not within Section 85E(1).

The definition of "business" in Section 139(1)(*e*) does enlarge the usual term "business" by the words "an adventure or concern in the nature of trade", but that enlarge-

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ment and its tests as seen in *Irrigation Industries Limited v. M.N.R.*[4] and in *M.N.R. v. Taylor*[5], have no application here, as the appellant must contend for a "business" with an "inventory", and hence the appellant is required to prove a "business" in the usual meaning of that term. That definition is as follows: In *Smith v. Anderson*[6] Jessel, M.R. stated at p. 258:

> That is to say, anything which occupies the time and attention and labour of a man for the purpose of profit is business.

and at p. 260:

> ... and I have no doubt if any one formed a company or association for the purpose of acquiring gain, he must form it for the purpose of carrying on a business by which gain is to be obtained.

In *Frankel Corporation Limited v. M.N.R., (supra)*, Martland J. quoted from *Californian Copper Syndicate v. Harris*[7] and stated at p. 255:

> Is the sum of gain that has been made a mere enhancement of value by realising a security, or is it a gain made in an operation of business in carrying out a scheme for profit-making?

In *Samson v. M.N.R.*[8] Thorson P. stated at p. 33:

> ... "the pursuit of a trade or business" involves the pursuit of gain or profit.

and see *M.N.R. v. Spencer*[9].

The transactions between the appellant and the employee shareholders were not for the purpose of gain. There was no intention of making a profit on the sale of the shares as those were sold at the same price as the appellant purchased from IMC. The contention is that the profit was in the interest charged and therefore to be a business the alleged financing business must have been carried on for the purpose of making a profit from the interest charged on monies lent.

The interest is taxable under section 27(1) because it is interest, not because it is a profit derived from "business" nor from the sale of "inventory" as required by section 85E(1). Therefore the fact of interest being taxable does not denote such interest necessarily arises from "business" or from the realizing of inventory; interest is not an absolute test of "business" or of "inventory".

[4] [1962] S.C.R. 346 at p. 352.

[5] [1956-60] Ex. C.R. 3; [1956] C.T.C. 189.

[6] (1880) 15 Ch. D. 247.

[7] (1904), 5 T.C. 159.

[8] [1943] Ex. C.R. 17.

[9] [1961] C.T.C. 109 at p. 133.

In any event, the appellant's charging of interest to the employee shareholders does not indicate that the appellant entered into a finance business for the purpose of making such a profit by that interest—or that the transactions with the employee shareholders were for a profit from the interest. The interest charged was $2\frac{1}{2}\%$ if the purchasing employee applied dividends up to 65%, otherwise $4\frac{1}{2}\%$. That rate of interest charged was initially the prime rate in Minneapolis but shortly thereafter the prime rate exceeded that charged and in Vancouver where the appellant kept its account in U.S. funds for the purpose of receiving these payments and also for the purpose of purchasing from IMC, the prime rate always exceeded that charged the purchasing employee. If a financing business had been carried on to produce a profit it would be expected that the appellant would have charged at least the prime rate, that is, the going rate, nevertheless the appellant has charged throughout the same rate even when that was less than the prime rate, the reason being, of course, to prevent discriminating against employees. The profit arose by reason of the circumstance that $2,700,000 was raised by the appellant selling its shares and only the balance as needed was borrowed; for borrowed monies the appellant paid interest at a higher rate than that charged to the purchasing employees. Accordingly, the profit is shown by charging only interest paid on the money borrowed but not showing any interest on the $2,700,000 realized from the sale of shares. By such method a profit could have been shown on paper if even a lesser rate than $2\frac{1}{2}\%$ had been charged. Exhibit A-5 shows the interest income to be $2,-183,945.83 and the interest expense, that is, on monies borrowed, $733,853.88. Exhibit A-6 shows the amount of average daily borrowings of the appellant from IMC and the rate of interest paid. The transactions between the appellant and the employee shareholders could not have been undertaken by the appellant for the purpose of gain from the interest charged the employee because:—

(1) The option with the employee shareholder at the book value and the option over to Bean at a stated price would result in a liability immediately of $315,000, later increasing to $345,000 and only later wiped out by Bean (Ex. R-6 and Ex. R-4).

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(2) The fixed interest in the agreement between the appellant and the employee shareholder ($2\frac{1}{2}\%$ with a possibility of $4\frac{1}{2}\%$) was less than the prime rate at Vancouver, B.C. where the appellant did its banking. The real purpose of the sale of the shares was therefore not profit from the interest charged. There was no profit over the prime rate of interest.

(3) The real purpose of selling shares in IMC to employees of IMC and of a subsidiary was to benefit the employees thereby benefiting the employer company, thereby ultimately benefiting those controlling IMC. But only two of the appellant's employees were shareholders of IMC at the time of the sale to the Bank, therefore there could have been no real or substantial benefit to the appellant through its buying and selling shares in IMC and certainly no such profit as would permit the inference that it was conducting a business, and particularly a financing business.

As the appellant was not carrying on a financing business, therefore by the sale to the First National Bank it was not "ceasing to carry on a business or part of a business" within section 85E(1), nor were these agreements sold to the First National Bank of Minneapolis "included in the inventory of the business" within section 85E(1).

M.N.R. v. Curlett[10], relied upon by this appellant, is distinguishable on the facts; there Curlett "patently was in the money lending business" and here the appellant was not in the money lending business.

Further, as the shares were capital, therefore the purchase price receivable from the employee shareholders was equally capital: *Frankel Corporation Limited v. M.N.R.*, (*supra*). Hence the appellant was selling and the Bank was purchasing a capital asset, therefore the price paid by the Bank resulted in a capital loss to the company, but such a loss is excluded by section 12(1)(*b*).

Section 85E(1) provides for the enlargement of taxable income by the inclusion of the sale of inventory referred to but does not provide for a deduction from taxable income. Therefore there is nothing in section 85E(1) to permit a

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[10] [1967] S.C.R. 280; [1967] C.T.C. 62.

deduction as is contended for by the appellant or to qualify the prohibition of deduction contained in section 12(1)(*b*).

The question whether or not the transactions between the appellant and the employees of other companies were *intra vires* of the appellant was not formally raised nor is it now decided.

In conclusion, the loss complained of by the appellant was a loss of capital and should not be deducted from the income as contended by the appellant.

The appeal is dismissed with costs.

Ottawa
1968
Jan. 29-30
Feb. 26

BETWEEN:

THE DRACKETT COMPANY OF CANADA LTD. .... APPELLANT (*Opponent*);

AND

AMERICAN HOME PRODUCTS CORPORATION .... RESPONDENT (*Applicant*).

Trade marks—Appeal from Registrar's decision—Opposition to registration—Proposed mark "Once-a-Week" applied to floor cleaner—Whether descriptive mark—No reasons given for Registrar's decision—Whether error in law—Trade Marks Act, s, 12(1)(b).

An application for registration of the proposed trade mark "Once-a-Week" to be used in association with a floor cleaner was opposed on the ground that it was "clearly descriptive or deceptively misdescriptive ... of the character or quality of the wares ..." and therefore not registrable under s. 12(1)(*b*) of the *Trade Marks Act* and on the further grounds that it was confusing with a trade mark of the opponent and that it was not distinctive. The opposition was rejected by the Registrar of Trade Marks as "not well founded" but he stated no reasons for that conclusion.

Held, on appeal, the Registrar erred in law in not holding that the expression "Once-a-Week" used in association with a floor cleaner would be clearly descriptive or deceptively misdescriptive of the character or quality of the floor cleaner. No person properly addressing himself to that question could come to any other conclusion.

Rowntree Co. v. Paulin Chambers Co. [1968] S.C.R. 134; *Benson & Hedges (Canada) Ltd. v. St. Regis Tobbacco Corp.* [1968] 2 Ex. C.R. 22 distinguished.

APPEAL from Registrar of Trade Marks.

William R. Meredith, Q.C. and *Donald G. Finlayson* for appellant.

Peter Thompson for respondent.

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CATTANACH J.:—This is an appeal pursuant to section 55 of the *Trade Marks Act*, chapter 49 of the Statutes of Canada, 1952-53, from a decision of the Registrar of Trade Marks under section 37 of that Act rejecting the opposition of the appellant to the respondent's application for the registration of a proposed trade mark "Once-a-week" to be used in association with a "floor cleaner".

The Registrar's decision, dated April 5, 1966 was expressed in the following terms:

> The applicant applied, pursuant to Section 16(3) of the *Trade Marks Act*, for registration of the trade mark "ONCE-A-WEEK" for use in association with a floor cleaner.
>
> The opponent opposed the application on the following grounds:—
>
> (a) The applicant is not entitled to registration in view of Section 37(2)(*b*) of the *Trade Marks Act* namely that the trade mark "ONCE-A-WEEK" is not registrable under Section 12(1)(*b*) since such trade mark is clearly descriptive or deceptively misdescriptive in the English and French languages of the character or quality of the wares with which the said trade mark is used or proposed to be used.
>
> (b) The Applicant is not entitled to registration in view of Section 37(2)(*c*) namely that the applicant is not the person entitled to registration in view of the provisions of Section 16(3)(*a*) by reason of the fact that at the date of filing of Application No. 279,739 for the trade mark "ONCE-A-WEEK" or at any date upon which the applicant is entitled to rely, the trade mark "ONCE-A-WEEK" was confusing with the opponent's trade mark "Once in Every Week DRANO in Every Drain" which the opponent had previously used in Canada and which the opponent's predecessor with respect to this trade mark, The Drackett Company, and the opponent had previously made known in Canada. The opponent intends to rely on a date of first use at least as early as November 1959 and intends to rely on making known at least as early as the said date of November 1959. In connection with making known in Canada, the opponent will also rely on the activity in the United States of its said predecessor, The Drackett Company, in relation to the trade mark "Once in Every Week DRANO in Every Drain" registered in the United States under No. 767,768 dated March 31, 1964.
>
> (*c*) The applicant is not entitled to registration in view of Section 37(2)(*d*), namely that the trade mark "ONCE-A-WEEK" is not distinctive since it is not adapted to distinguish the wares which the applicant proposes to associate with it from the wares which the opponent associates with the trade mark "Once in Every Week DRANO in Every Drain".
>
> I have considered the evidence on file, the written arguments as well as the representations of counsel for both parties at a hearing held March 29th, 1966 and have arrived at the conclusion that the grounds of opposition are not well founded. Accordingly, the opposition is rejected pursuant to Section 37 of the *Trade Marks Act*.

The evidence before the Registrar consisted initially of the respondent's application for registration of a proposed trade mark dated December 27, 1963, on a prescribed form, stating that the trade mark applied for is the words "Once-a-Week" and that the applicant intended to use that mark in Canada in association with a floor cleaner. It is clear from the fact that the application was for a proposed trade mark and from the applicant's statement that it intended to use the mark in association with a floor cleaner, that there had been no prior use of the trade mark by the applicant.

By letter dated March 3, 1964 the Registrar advised the applicant, in accordance with the duty imposed upon him by section 36(2) of the Act, that he considered the proposed trade mark to be clearly descriptive or deceptively misdescriptive of the character "and/or" quality of the wares in association with which it was proposed to be used and that, therefore, the mark did not appear to be registrable in view of the provisions of section 12(1)(*b*) of the *Trade Marks Act*. The applicant was advised that any comments it wished to make would be given consideration, which was also the statutory obligation of the Registrar to do.

Pursuant to that invitation, representations were made on behalf of the applicant by its solicitors in a letter dated April 1, 1964 which apparently resulted in the Registrar not being satisfied that the proposed trade mark was not registrable because he then caused the application to be advertised in the manner prescribed.

The appellant herein thereupon filed a statement of opposition based on the three grounds as set out in the Registrar's decision quoted above.

The respondent, as applicant, filed a counter-statement.

The appellant, as opponent to the application, filed evidence in the form of two affidavits of F. S. Knox, the president of the appellant company, one of which affidavits had annexed thereto, six exhibits being copies of advertisements of its product, "Drano", in publications extensively circulated in Canada and featuring words and slogans such as "Make one day a week Drano day"; "Drano once a week keeps drains trouble free"; "Use Drano once a week in every drain" and "once in every week Drano in every drain".

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The other affidavit of F. S. Knox had annexed ten exhibits being photostatic copies of story-boards used in actual television commercials which featured similar words and slogans as appeared in the published advertisements exhorting prospective purchasers to use its product, "Drano", weekly.

The two foregoing affidavits establish that the appellant, long engaged in the manufacture and sale of its product under the trade mark "Drano", consistently stressed in its advertising of that product on network television programs and in consumer magazines the theme that its product should be used on a weekly basis.

Incidentally the product, "Drano", is a chemical compound for cleaning, clearing and opening the drains of sinks, washboards and the like.

There was no evidence whatsoever as to the respondent's product other than the bare statement in the application for registration of the proposed trade mark that it is a "floor cleaner". Conceivably it might be a cleansing agent exclusively, or a cleansing agent in combination with some protective property. Neither was there any evidence of its applicability to the variety of flooring in modern use, that is whether its use is restricted to a particular type of flooring or is useful with respect to all types. Further there was no information as to whether the product was designed for use on areas of heavy, modest or light traffic or all such areas.

The respondent, as applicant, was not under any obligation to, nor did it file any evidence.

Therefore the only evidence before the Registrar was the application itself and the two affidavits above. There was also before him the written argument on behalf of the contending parties in the statement of opposition and counter-statement and he had, in addition, the benefit of oral argument by counsel for both parties at the hearing before him.

In argument before me counsel for the appellant abandoned the second ground of opposition that was advanced before the Registrar, namely, that the respondent was not entitled to registration under section 37(2)(*c*) of the Act because the proposed trade mark "Once-a-Week" was confusing with the appellant's trade mark "Once in Every

Week Drano in Every Drain" previously used in Canada and which the appellant's predecessor had previously made known in Canada. In so doing counsel for the appellant stated that the expression "Once in Every week Drano in Every drain" was not the subject matter of a registered trade mark in Canada. It did appear, however, that The Drackett Company, the appellant's predecessor, had registered the expression in the United States as a trade mark in which jurisdiction slogans appear to be registrable. I construe counsel's withdrawal of this ground of opposition as an admission that the expression in question, excepting the word "Drano", has not been used and is not known as a trade mark in Canada.

The contention of counsel for the appellant before me was, as I understood it, twofold, (1) that the proposed trade mark is not registrable within section 37(2)(*b*) in that it is "clearly descriptive or deceptively misdescriptive in the English or French languages of the character or quality of the wares or services in association with which it is used or proposed to be used..." and so within the prohibition of section 12(1)(*b*) and, (2) that the proposed trade mark is not distinctive within the meaning of section 37(2)(*d*).

The contrary contention advanced by counsel for the respondent was that the proposed trade mark "Once-a-Week" is not "clearly descriptive of the character or quality" of a floor cleaner but is, at most, merely suggestive or meaningless when so associated and that the mark is capable of being adapted to distinguish the respondent's wares from those of another and is, therefore, "distinctive" within the relevant portion of the definition of that word in section 2(*f*) of the Act.

If the responsibility for the initial decision had been mine, I would have concluded that the proposed trade mark was not registrable under section 12(1)(*b*). I think that the words "Once-a-Week" are merely informative, descriptive or generic as applied to a floor cleaner and that such words are not likely to serve any purpose other than to inform prospective purchasers of the frequency with which the product should be used.

In so concluding, I accept without question the submission of the respondent that the decision that a trade mark is clearly descriptive is one of first impression.

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My first impression, and my continuing impression, is that the words "Once-a-Week" would convey to a prospective purchaser and immediately identify a floor cleaner with which it is associated as one that need be used only once a week and that one application thereof would endure for that period of time.

The word "clearly" in section 12(1)(*b*) of the Act, which precludes the registration of a trade mark that is "clearly descriptive...of the character or quality of the wares or services in association with which it is used or proposed to be used", is not synonymous with "accurately" but rather the meaning of the word "clearly" is "easy to understand, self-evident or plain".

It is not a proper approach to the determination of whether a trade mark is descriptive to carefully and critically analyse the word or words to ascertain if they have alternative implications when used in association with certain wares but rather to ascertain the immediate impression conveyed thereby. I do not accept the submission of counsel for the respondent that the words, "Once-a-Week" are merely suggestive of the results to be obtained. I think the use of such mark goes further than that. A person faced with a floor cleaner described as "Once-a-Week", in my opinion, would assume that the product need only be used weekly and would endure for that period of time which, to me, is an attribute or property that has a direct reference to the durable and excellent quality of the product. Further the word "character" as used in section 12(1)(*b*) must mean a feature, trait, or characteristic of the product. The proposed trade mark "Once-a-Week" clearly implies that the product with which such mark is associated is to be used weekly. This, to me, is a direct reference to the "character" of the product. For the same reasons I do not accept the submission that the words "Once-a-Week", when associated with a floor cleaner are meaningless. As applied to the product in question the words to be meaningless should be so obviously and notoriously inappropriate as to be not calculated to suggest description which, in my view, is not the case here. I feel that the meaning of the words is abundantly clear.

Since I would come to a conclusion diametrically opposed to that of the Registrar, that the grounds of opposition to the registration of the proposed trade mark, "Once-a-Week" are not well founded, the question arises whether it is open to me to substitute my conclusion for his and allow the present appeal.

The nature of this Court's duty was considered by the Supreme Court of Canada in *The Rowntree Company Limited v. Paulin Chambers Co. Ltd.*[1] In that case there was an appeal from the decision of the Registrar that a trade mark, the registration of which was sought, would be confusing with an existing trade mark, the concurrent use of which would lead to the inference that the wares of the conflicting parties emanated from the same source. This Court substituted its view on the issue whether the marks were confusing and on appeal to the Supreme Court of Canada, that Court by a unanimous judgment delivered by Ritchie J. allowed the appeal and restored the Registrar's decision. Ritchie J. said:

> It is contended on behalf of the respondent that the conclusion reached by the learned trial judge should not be disturbed having regard to the terms of s. 55(5) of the Act which provides that "on the appeal... the Court may exercise any discretion vested in the Registrar". I do not, however, take this as meaning that the Court is entitled to substitute its view for that of the Registrar unless it can be shown that he proceeded on some wrong principle or that he failed to exercise his discretion judicially.
>
> ...
>
> In my view the Registrar of Trade Marks in the present case applied the test required of him by the statute and I do not think that grounds were established justifying the learned judge of the Exchequer Court in interfering with his conclusion. For all these reasons I would allow this appeal and restore the decision of the Registrar of Trade Marks refusing the respondent's application S.N. 264951.

The President of this Court rendered a decision in *Benson & Hedges (Canada) Limited v. St. Regis Tobacco Corporation*,[2] which was also an appeal from a decision of the Registrar on the similar issue as to whether two trade marks were confusing. Although he would have reached a contrary decision to that of the Registrar, he concluded, in the circumstances of the case before him, that it was not open to him to substitute his decision for that of the Registrar on the authority of the *Rowntree* case. He added:

> In this case, no submission has been made that the Registrar proceeded on a "wrong principle" or "that he failed to exercise his

[1] [1968] S.C.R. 134.

[2] [1968] 2 Ex. C.R. 22

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> discretion judicially" and I know of no basis upon which any such submission could have been made. Not only is there no indication that he failed to follow the requirements of any provision in the statute, but there is no room for suggesting that he left out of account any material fact (Presumably the situation would be different if, under section 55(5) of the *Trade Marks Act,* additional evidence were adduced in this Court that made a difference of substance between the facts before the Registrar and the facts before this Court. Compare *The Queen v. Secretary of State,* [1953] 1 S.C.R. 417, per Locke J. at pages 425-6.) or came to any conclusion on the facts that could not be supported on the evidence. Certainly, there is no room for suggesting that he did not act judicially. That being so, there is no occasion for this Court to interfere with his conclusion and substitute its decision for his.

In the present appeal counsel for the appellant did submit that the Registrar had proceeded on a "wrong principle", that "he failed to exercise his discretion judicially", that his conclusion on the facts could not be supported on the evidence before him and that he gave no reasons for his decision as it was his obligation to do by virtue of section 37(8).

In contradiction counsel for the respondent submitted since the issues of whether a proposed trade mark is clearly descriptive of the character or quality of the wares with which it is to be associated and whether a proposed mark is adapted to distinguish those wares are both matters of first impression and accordingly the Registrar could say no more than he did. He further submitted that there was evidence before the Registrar upon which he could reasonably find as he did and, therefore, his decision cannot be reviewed.

I have looked at the language employed by the Registrar in stating his conclusion in an attempt to ascertain whether he attached the weight he should have to the material before him, or whether he rejected material which he should have considered and in short to determine if he arrived at his conclusion judicially.

I have been unable to obtain any assistance therefrom. After identifying the proposed trade mark and the product with which it was to be associated, reciting the three grounds of opposition to its registration and stating that he considered the evidence on file, the written and oral representations on behalf of the respective parties, he then announced his conclusion that "the grounds of opposition

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are not well founded" and rejected the opposition. Other than that he did not elaborate upon the grounds by which he reached that conclusion.

Having regard to the nature of the application, the simple question that the Registrar had to decide under section 12(1)(*b*) of the Act was whether the expression "Once-a-Week" used in association with a "floor cleaner" would be clearly descriptive or deceptively misdescriptive of the character or quality of the floor cleaner. Making every allowance for the possibility of different minds reacting differently to the same set of circumstance, I cannot escape the conclusion that the Registrar erred in law in not holding that it would be. Just as no person, properly addressing himself to the question to be decided, could come to any conclusion with reference to a word such as "tender" used in association with meat, except that it is clearly descriptive or deceptively misdescriptive within the meaning of section 12(1)(*b*), so, in my opinion, no person, properly addressing himself to the question to be decided, could come to any conclusion with reference to the expression "Once-a-Week" used in association with a floor cleaner, except that it is clearly descriptive within the meaning of section 12(1)(*b*).

It follows that I must conclude that the Registrar misconceived the question that he had to decide when considering that branch of the case and is manifestly wrong.

Having reached that conclusion, there is no need to decide whether the other attack on the application for registration, that is, that the proposed trade mark is not capable of being adapted to distinguish the respondent's product and is therefore not distinctive, should have succeeded.

The appeal is allowed with costs and the matter is referred back to the Registrar for appropriate action in accordance with these reasons.

Montreal 1968 Jan. 24-25 — Ottawa 1968 Feb. 27

BETWEEN:

EUGÈNE LAGACÉ .... APPELLANT;

AND

THE MINISTER OF NATIONAL REVENUE .... RESPONDENT.

AND

BETWEEN:

GEORGES LAGACÉ .... APPELLANT;

AND

THE MINISTER OF NATIONAL REVENUE .... RESPONDENT.

Income tax—Business profits—Computation of—Profits channelled to controlled company—No bona fide business transaction—Contract requiring profits to be used to pay debts of controlled company—To whom profits chargeable—Acquisition of interest in option on lands—Allowance for cost in computing profits—Income Tax Act, ss. 3, 4.

Appellants, who with *F* had acquired options on certain lands which they intended to turn to account at a profit, later acquired *F*'s interest in the options on terms that the options be taken up by one of two companies controlled by appellants and the profits therefrom applied if necessary to discharge that company's debts, which *F* had guaranteed. The lands were disposed of by appellants in a complicated series of transactions involving the two companies controlled by them. The total profit accruing to appellants and the two controlled companies from the transactions was $150,765, but appellants each reported as his share thereof only $5,642 which was based on the price at which appellants transferred the options to the two controlled companies. No evidence was given that any of the profit from the transactions was applied on one of the controlled company's debts in accordance with appellants' agreement with *F*.

Held, appellants were chargeable to income tax on the $150,765 profit which accrued both to themselves and the controlled companies

1. A trader cannot reduce the profits from his trading transactions for purposes of income tax by merely substituting for a conveyance between himself and a third party a series of conveyances involving companies under his control which do not represent *bona fide* business transactions.

2 Even if the profits from the transactions were used to pay debts of a company controlled by appellants, as required by their contract with *F* (as to which there was no evidence), such profits remained profits from appellants' business operations and therefore were chargeable to tax in their hands.

3. In the absence of any evidence to establish the cost to appellants of acquiring *F*'s interest in the options no allowance could be made for

such cost in computing appellants' profits. That cost might be an appropriate part of the amount paid out of such profits on the controlled company's debts pursuant to the contract with *F* or, if it could be determined, it might be the value of the consideration given *F* for his interest in the options, but, failing evidence of these, would appear to be the amount of the disbursements made as a result of the agreement with *F*, as to which there was no evidence *Harrison v John Cronk & Sons, Ltd.* [1937] A.C. 185 and *Absalom v. Talbot* [1944] A.C. 204, referred to.

INCOME TAX APPEALS.

Philip F. Vineberg, Q.C. for appellants.

Jean-Claude Sarrazin and *A. Garon* for respondent.

JACKETT P.:—These appeals from decisions of the Tax Appeal Board dismissing appeals from the appellants' assessments under Part I of the *Income Tax Act* for the 1958 taxation year were heard together in Montreal on January 24 and 25, 1968.

In each case, the respondent had assessed the appellant on the basis that his share of the profits from certain transactions relating to the acquisition and disposition of lands at Fabreville, Quebec, was $75,382.60, and not merely the lesser amount of $5,642.50 shown by the appellant in his income tax return for the taxation year.

The questions raised, in each case, by the Notice of Objection to the assessment and by the Notice of Appeal to the Tax Appeal Board were (a) whether the appellants' profit from such transactions was $5,642.50 as contended by the appellant or $75,382.60, as found by the respondent, and (b) whether the profit was, in either case, subject to income tax. (There has never been any question raised as to the correctness of the amounts assuming taxability on one basis or another.)

The appellant's position, in each case, at each of those stages, was that the two appellants and one Fortin had, in 1956, acquired certain options to buy land at Fabreville and that each of the appellants had, in 1958, transferred his share in the options to a company for a consideration of $15,000, which, after deduction of his expenses, had yielded him a profit on the transaction of $5,642.50, the amount reported by him as income.

What the respondent had learned before the assessments appealed from is that the appellants had (after acquiring

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Fortin's interest in the options) not only entered into the transactions during the latter part of 1958 under which they had each received a gross amount of $15,000, but they had, during the same period, caused companies under their control[1] to enter into transactions relating to the land at Fabreville as a result of which the total net profit accruing to the appellants and companies under their control as a result of the acquisition and disposal of the Fabreville lands was $150,765.20. It was apparent that all the actual bargains involved (that is, bargains between the appellants or companies under their control on the one hand and persons with whom they were dealing at arm's length on the other) were negotiated by the appellants with the persons with whom they were dealing at arm's length, and that the appellants subsequently arranged for the various intervening conveyances under which a large part of the profits arising from the dispositions were made to appear as having accrued to companies under the control of the appellants and not to the appellants.

In these circumstances, it seems, although he did not express himself as clearly as he might have done, that the respondent took the position in making the assessments appealed from that the transactions giving rise to the profit of $150,765.20 were either (a) exclusively those of the appellants on their own account (the companies under their control having been used merely as instrumentalities through which implementing conveyances and other operations were carried out[2]), or (b) in part those of the appellants and in part transactions associated with other transactions that brought into play section 16(1), section 17(2), or section 137 of the *Income Tax Act*. On the first

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[1] The companies referred to as companies under the control of the appellants in these reasons are E. & G. Lagacé Inc. and Adrien Lagacé Inc. While no clear evidence has been forthcoming as to the shareholding in these companies, it is clear that, at least from early 1958, each of the companies was controlled by some or all of the two appellants and their wives

[2] In this connection, it is to be noted that the evidence of the appellants, particularly that of Georges Lagacé, shows that it was common practice for the appellants so to use E. & G. Lagacé Inc In his evidence before the Board, after he said that the options belonged to the three individuals (Fortin, his brother and himself), he was asked why E. & G. Lagacé Inc had paid for them and he replied: «Bien, mon Dieu, on a toujours fait nos affaires par la compagnie ou par la compagnie E & G Lagacé Inc.»

alternative, if it were correct, each of the appellants was, of course, properly taxed on his share of the total profit (assuming it was a profit from a "business" within the meaning of the *Income Tax Act*) just as any trader would be if, for some reason, his trading transactions were carried out through, and in the name of, a trust company, bank or other nominee acting as his agent or trustee.

Apparently, after hearing the evidence adduced before him, Mr. Boivert, the member of the Tax Appeal Board by whom the appeal was heard, took that view of the transactions because he said:

> Les faits, à première vue, semblent bien enchevêtrés A les examiner de près, il est facile de se rendre compte qu'ils ont été agencés de façon à constituer un trompe-l'œil pour le répartiteur pensant sans doute qu'il était atteint de myopie, ce qui n'était pas le cas.

Whether or not the appellants thought that the assessor "était atteint de myopie", the basis upon which the appeal to the Tax Appeal Board was launched appears to have been a view that a trader may reduce the profits from his trading transactions (at least for purposes of income tax) by merely substituting for a straightforward conveyance between himself and the person with whom he has negotiated a transaction a complicated series of conveyances involving companies under his control, even though such conveyances do not represent *bona fide* business transactions. This seems clear from the fact that, while the assessments appealed from were obviously based on transactions in the names of companies under the control of the appellants, the appellants did not consider it necessary for their case, that they, by the various documents in which they were required to state the material facts or by the evidence before the Board, inform the Minister or the Board of the various transactions and establish that each of them was an actual *bona fide* contract that was in fact negotiated, by or on behalf of the persons named as parties, at the time of the negotiation of the business bargain. (Indeed, there is no suggestion anywhere in the documents or the evidence before the Board or in this Court[3] that either of the

[3] It is particularly significant that, after the clear findings of fact by the Board that the profits were profits from a business carried on by the appellants and were not profits from a business carried on by one of their companies, the appellants refrained from bringing any evidence in this Court to show actual trading transactions by either of the companies.

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controlled companies in question—E. & G. Lagacé Inc. and Adrien Lagacé Inc.—was engaged at the relevant time in a business of trading in land or that the appellants, in negotiating the various acquisition and disposition transactions with the third parties, were doing so as agents or employees of one or other of the companies controlled by them.)

The view to which I have referred, upon which the appeal appears to have been launched to the Tax Appeal Board, appears to me to be so clearly wrong that there is no need to give any reasons for so holding. As will appear subsequently, the appellants, in attempting to support their position, brought in additional evidence before the Tax Appeal Board on the basis of which the Board held, in a judgment with which I agree, that the profits in question were in fact profits from the appellants' own business transactions and that they had, in effect, received them and used them for their own purposes.

(The alternative position, to be found in the Notice of Objection and in the Notice of Appeal to the Tax Appeal Board, that the transactions in question were not trading transactions and that the appellants are even entitled to a return of the tax paid on the lesser amounts shown in their tax returns, was not pressed before the Tax Appeal Board and was expressly dropped before me by counsel for the appellants.)

However, according to counsel for the appellants, a new element in the story appeared for the first time in evidence presented to the Tax Appeal Board. On that occasion, for the first time, the appellants put forward a contract that they had made with Fortin in December 1957, which, they said, explained why one of the companies controlled by the appellants had been introduced into the transactions in question.

To understand the contract of December, 1957, it becomes necessary to refer to some facts that were not otherwise material.

The appellants, who are brothers, had three other brothers who, prior to 1958, owned the shares in the company known as Adrien Lagacé Inc., which company had carried on a substantial housebuilding business at Beaconsfield, Quebec. Early in 1957, Adrien Lagacé Inc. having got into financial difficulties, Fortin (the man who had joined with the appellants in acquiring the Fabreville options) had guaranteed that company's indebtedness at the Bank up to an amount of $136,000. Shortly thereafter, Fortin took a conveyance of substantially all the assets of Adrien Lagacé Inc., which were at Beaconsfield, and undertook the task of liquidating them and using the proceeds to pay the company's creditors, who, of course, included the Bank. When he entered into this affair, Fortin seems to have thought that the company's problem was a temporary shortage of ready cash and there is no suggestion that he had any idea, at the commencement of his involvement in the affair, that the company's assets were not sufficient to pay all of its debts.[4] However, after working at the task for several months, Fortin found that it was taking longer, and involved more work, than he had expected. (He probably began to be concerned as to whether the proceeds of liquidation would be sufficient.) Having regard to his age and other responsibilities, he decided to try to get free of the matter. It was in these circumstances that he negotiated the contract of December 1957 with the appellants. That contract reads as follows:

> Entente entre Georges & Eugène Lagacé et J. M. E. Fortin tous de Dorval. Il est convenu entre les trois parties, ci-haut mentionné, que J. M. E. Fortin consent à céder tous ces droits dans huit options d'achat de terres situé à Fabreville, paroisse de Ste-Rose pour le prix de 1.00 dollar aux conditions suivantes.
>
> Étant donné que J. M. E Fortin est engagé envers la Banque Canadienne Nationale à Pointe Claire pour la Co. Adrien Lagacé Inc.
>
> Il est explicite que les dite options, lorsqu'ils seront exercer soit acheter en faveur d'Adrien Lagacé Inc. de maniere à libérer totalement J. M. E. Fortin de la Co. Adrien Lagacé Inc. que ce soit la banque ou toute autres créditeurs de la dite Co. Il est entendu que la balance des terrains de Beaconsfield appartenant à J. M. E. Fortin pour cause d'endossement envers Adrien Lagacé Inc. soit transférer par contrat notarié à Eugène ou Georges Lagacé ou tout autre Co. désigné par eux. Cette entente deviendra nul et sans effet si les obligations ci-haut mentionés ne sont pas respectées dans les douze mois de cette date.

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[4] Fortin said before the Tax Appeal Board:

«Après avoir fait 'rechecker' l'audition de leurs livres, je vois que leur position n'est pas très bonne. Il y avait du danger pour eux de faire banqueroute à moins qu'ils aient un peu de 'cash'. J'ai été voir la banque Canadienne Nationale de Pointe-Claire, Adrien Lagacé Inc. devait déjà à la banque Canadienne Nationale cent mille dollars ($100,000.00). Pour pouvoir passer à travers, ça prenait un autre quarante mille dollars ($40,000 00). J'ai vu un agent à la banque, j'ai dit: 'Donnez à Adrien Lagacé Inc. quarante mille dollars ($40,000.00) je vais endosser'.»

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By the contract of December, 1957, between Fortin and the appellants, as I understand it, Fortin agreed

(a) to turn over to the appellants or their nominee the company's Beaconsfield assets, which were, of course, dedicated to payment of the debts of Adrien Lagacé Inc.,[5] and

(b) to transfer to the appellants his one-third interest in the Fabreville options[6] on terms that the options should be taken up in the name of Adrien Lagacé Inc. to the extent necessary to vest in that company such part of the profits arising from turning the options to account as might be necessary to enable it to pay any part of its debt to the Bank that would not otherwise be paid and which, if not paid otherwise, would be payable by Fortin as a result of his guarantee.

Quite apart from the very substantial consideration (Fortin's one-third interest), the appellants were motivated to some extent in entering into this agreement by the fact that, while they profess to have had no legal obligation to stand behind their brother's company, and while Fortin was legally liable to do so, they recognized some moral responsibility because the company was their brother's company.

As I have already indicated, as I view the contract of December 1957, Fortin agreed to turn over to the appellants his share in the Fabreville options (which, as is conceded in this Court, had been acquired for the purpose of turning them to account at a profit in one way or another and which had substantially increased in value between the time of their acquisition in 1956 and December 1957) in return for a covenant by the appellants that they would utilize such part of the profits to be realized

[5] The notarial deed under which Fortin acquired these assets from Adrien Lagacé Inc. and the notarial deed whereby he transferred them to the appellants' nominee, E. & G. Lagacé Inc., each purport to be purchase transactions involving the payments of large sums of money. The evidence would indicate that no such amounts were paid or contemplated. No explanation that I can understand was offered for this anomaly.

[6] According to Fortin's evidence, he was at the same time freed from reimbursing E. & G. Lagacé Inc. for his share of the cost of the options, which had been paid by that company for Fortin and the appellants.

from the options as might be necessary to ensure that the company's debt to the Bank would be paid without Fortin being liable on his guarantee. (This might be an appropriate place to interject that, as it appears to me, the covenant to have the options taken up in the name of the company was merely the method adopted to carry out the obligation of turning over some part of the profits to the company.)

About the end of 1957, and before any steps were taken to turn the options to account, the three Lagacé brothers who had owned the shares in Adrien Lagacé Inc. transferred such shares to the two appellants and their wives or to one or more of them.[7] The result was that, while the company had been controlled up to December 1957 by the three Lagacé brothers who are strangers to these appeals, it was, during the course of the 1958 transactions that gave rise to the profits that are the subject of these appeals, a company all the shares of which belonged to one or other of the appellants or their wives.

In this Court, in the light of the December 1957 contract, it was contended on behalf of the appellants, in effect, as I understand it, that the profits in dispute were not the appellants' profits because the appellants were required by that agreement so to arrange the transactions that the profits would vest in Adrien Lagacé Inc. and that they had in fact done so with the result that the profits vested in the company and not in the appellants.

I reject this contention for two reasons, *viz*:

(a) the onus was on the appellants to establish, as a factual basis for this contention, that the profits in dispute had, in fact, been used, as contemplated by the agreement, to pay such part of the debt of Adrien Lagacé Inc. to the Bank as could not be paid out of the company's own assets (the Beaconsfield assets) and the appellants have completely failed to prove that any part of such assets were so used, and

[7] According to an assessor's reports that are part of the evidence by consent of counsel, Mrs. Georges Lagacé became owner of all of the ordinary shares and the two appellants received preferred shares, the only consideration being Mr. Lagacé's guarantee of company debts in the amounts of $8,000. The same reports say that the company re-acquired the preferred shares from the appellants for cash after the company had received some of the proceeds from the Fabreville transactions.

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(b) even if the whole of the profits in dispute had been so used, that would not change their character as profits arising directly from the appellants' business operations.

I shall deal first with the appellants' failure to establish the factual basis for their contention.

In that connection it is important to consider first what had to be proved. As I understand the December 1957 contract, Fortin agreed to turn over to the appellants or to their nominee the balance of the Beaconsfield assets of the company that he had been in the process of liquidating so that he might use the proceeds to pay the company's debts.[8] Obviously, under the arrangement, the appellants were to continue this process and they were only bound by the contract to use the profits from the Fabreville options to pay the company's debts if, and to the extent that, the proceeds of the Beaconsfield properties were inadequate for the purpose. What the appellants had to prove, therefore, was

(a) that the proceeds of disposition of the Beaconsfield property had been insufficient to pay some part of the company's debt to the Bank,

(b) the amount that had been left owing to the Bank after all the monies available from the Beaconsfield assets of the company had been paid to the Bank, and

(c) that that amount had been paid to the Bank out of the Fabreville profits.

Having regard to the manner in which the question arises and the substantial amounts involved, it was not in my view sufficient for the appellants to testify simply that they knew that all the Fabreville profits had been used to pay off the company's debt at the Bank and that there had been a loss on the liquidation of the Beaconsfield assets, but that they really had no knowledge of just what was done in respect of either matter, or who did it or how it was done. That, however, is in reality the gist of their

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[8] I accept it that this was the intent notwithstanding the unexplained form of the notarial conveyances, which were so framed as to indicate sales for substantial prices.

evidence. Indeed, in the first place, no evidence was put forth on behalf of the appellants on either matter; and, when asked about some aspects of the matters on cross-examination, they indicated a lack of any knowledge of what had really happened.

The very simple position put forward on behalf of the appellants during the hearing in this Court was that there was, at the relevant time, $136,000 owing to the Bank, that there was approximately the same amount of profits from the Fabreville transactions (apart from the amounts that they showed as having been received by them personally), and that, while there was no direct evidence as to what had actually happened, it should be inferred that such profits were used to pay the debt to the Bank.

Even if such an inference would be a fair inference to draw from those facts if they had been established and everything else had been left untold, that is not the state of the record. It is quite clear from the evidence that, while the Bank debt had been $136,000 on February 8, 1957 (paragraph 2(d) of the agreement of facts), it was, according to the Bank statements that were put in evidence, reduced to $109,000 by March 1958, which was long before the transactions giving rise to the profits in question. Apart entirely from this substantial difference between the facts on which the appellants' contention is based and the evidence, where there is evidence, a comparison of the payments to the Bank, as shown by the Bank statement, with the payments to the companies controlled by the appellants as shown by the various conveyances, which show the payments very precisely indeed, not only fails to lend any support for the appellants' contention, but suggests strongly that a large part of the monies from the Fabreville transactions did not go directly to the Bank and that the monies that were used to pay the Bank must have come, immediately at least, from somewhere else.

When one turns to consider what happened in connection with the liquidation of the company's own assets at Beaconsfield, there is simply no information except bald assertions that they gave rise to a loss. I find it impossible to accept these assertions without something more specific by way of explanation. A comparison of the figures in the conveyance of these properties from the company to Fortin with the figures in the conveyance from Fortin to the company controlled by the appellants, as well as an examination of the record of payments to the Bank would suggest that liquidation of the company's own assets had been resulting, during Fortin's administration and during the administration by the appellants prior to the realization of the Fabreville profits, in substantial payments on the company's debts. I know of no reason to think that the process of liquidation had been completed before the Fabreville transaction and I am not prepared to make a finding on the evidence before me that it had ceased to yield anything for payment of debts some time in the early part of 1958. If that had been so, I should have thought that the appellants could have shown, by evidence in the Tax Appeal Board or in this Court, what actually happened.

I am, therefore, not able to make a finding that any part or all of the profits arising from the Fabreville properties were used to pay the debt to the Bank in accordance with the terms of the agreement of December 1957.

Before parting with this branch of the case, I might make the comment that, where the onus is on a party to prove something within his knowledge or concerning his own business affairs, it is incumbent on him either to put a reasonably complete, and completely documented, story before the Court, so that it may be tested by cross-examination, or to explain to the Court why such evidence is not available. The failure to take one or other of those steps must always weigh heavily in the balance against such a party when the party contents himself, as the appellants did here, with a submission that an inference should be drawn from certain very sketchy facts as to what the party himself actually did. Here, of course, I have held that the facts on the basis of which I was asked to draw the inferences have not been established. However, even if they were established, I should have had to consider where the balance of probability lay when the parties had seen fit not to give the full story with appropriate documentation or to show that they could not do so.[9] I am inclined to think

[9] Even if the appellants did not personally handle the Beaconsfield transactions or the Fabreville transactions in sufficient detail to be able, by reference to the records, to show what happened, their bookkeeper, or other person who handled the matters on their behalf, must have been able, if available, to do so.

that, ordinarily, my conclusion would be that the full story was withheld because it was unfavourable to the party who withheld it.

I turn now to my second reason for rejecting the contention put forward on behalf of the appellants, which I repeat here for convenience. It is that, even if the whole of the profits in dispute had been used to pay the debt of Adrien Lagacé Inc. to the Bank because the appellants were required by their agreement with Fortin so to use them, that would not change their character as profits from the appellants' business operations.

The most significant feature of the appellants' contention in this Court, as it strikes me, is that it is inherent in the contention that profits that would otherwise have accrued to the appellants have ended up in the name of a company controlled by them, not because of *bona fide* business transactions between the appellants and such company, but because of transactions that have been arranged between them to implement a contract between the appellants and a third person to accomplish objects desired by the third person. In other words, the contention is based on the assumption that profits of the appellants' business operations were put into the hands of the company by a device and that the profits were not the result of the company having embarked on business transactions. In my view, therefore, the short answer to the contention, even assuming the facts to have been established, is that, for purposes of Part I of the *Income Tax Act*, profits from a business are income of the person who carries on the business and are not, as such, income of a third person into whose hands they may come. This to me is the obvious import of sections 3 and 4 of the *Income Tax Act* and is in accord with my understanding of the relevant judicial decisions.

Having regard to my conclusion, as indicated above, that there were no *bona fide* business transactions between the appellants and the companies controlled by them, there is no occasion to deal with the respondent's alternative arguments based on sections 16, 17 and 137 of the *Income Tax Act*.

Another argument was made before me on behalf of the appellants to which I should make reference. It was argued

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that, even if the profits in question were income of the appellants, the amounts of the assessments are excessive in that no allowance has been made in their computation for the cost to the appellants of acquiring Fortin's share in the options. Superficially, there would appear to be merit in the contention. I cannot, however, find that the appellants put forward any evidence on the basis of which any such allowance can be made. On the one hand, such allowance might have been an amount equal to all or one-third (I need not decide which) of the amount paid out of the profits in question to the Bank under the December 1957 agreement but, as I have decided, the appellants have failed to prove that there was any such amount. On the other hand, if one could put a value on the consideration passing from the appellants to Fortin for his interest in the options, that amount might be allowed. There is, however, no evidence before me on which such value can be determined and I doubt whether it would be commercially practical to evaluate such a consideration. That being so, I am inclined to the view that the only allowance that could be made is the actual disbursements made as a result of the agreement.[10] The appellants have, as it seems to me, had full opportunity to establish such amounts and have chosen not to do so.

One other point taken by the appellants throughout the proceedings may also call for some mention. That is the suggestion that the appellants should not be required to pay income tax on the profits from the Fabreville transactions of 1958 because Fortin had not been assessed in respect of any part of them. There is, in my view, no substance in the point. Even if there were an omission by the respondent to assess a third party for income tax on his profits arising from the same facts, that is no ground for invalidating an assessment that is otherwise valid. Here, of course, Fortin was no party to the transactions of 1958 giving rise to the profits in question as he had parted with all his interest in the options in 1957. Whether or not he made a profit in respect of which he should have been taxed by reason of his acquisition in 1956 and disposition in 1957 is a completely different question.

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[10] Compare *Harrison v John Cronk & Sons, Limited,* [1937] A.C. 185, and *Absalom v. Talbot,* [1944] A.C. 204, where similar problems concerning revenue items are discussed.

I have not overlooked the argument based on section 85B of the *Income Tax Act*. Although no reference is made to a claim under that section in the Notice of Appeal, and there is no evidence before me on which I could direct an allowance under that section, I would be prepared to entertain a motion to amend the notice of appeal so as to provide a basis for a judgment referring the assessments back for re-assessment on this point. It may be however that, having regard to section 85B(1)(*e*), such a motion should not be allowed.

If no such motion is made within three weeks from the date of these reasons, judgment will be pronounced dismissing the appeals with costs.

APPENDIX

So that there may be no misunderstanding as to the view upon which I have acted in deciding this case, I should like to make it clear that, as I see it, there is a clear distinction in principle between

(a) the case where a trader carries out business transactions of his business in the name of some other person who is agent, trustee or "nominee", in which case, the profits from selling his "stock-in-trade" are profits of his business even though the transactions are carried out in the name of somebody else, and

(b) the case where a trader takes stock-in-trade out of his business and uses it himself or gives it to somebody else so that there is no sale of it in the course of the business and can therefore be no profit from a sale of it in the course of his business.

In this case, I came to the conclusion, after examining with care a very confused record, that the business transactions giving rise to the profits in question were really those of the appellants.

If this had been a case where the stock-in-trade (the options) had been taken out of the appellants' business and given away to somebody else, such cases as *Sharkey v. Wernher*[11], *Petrotim Securities, Ltd. v. Ayres*[12], and *Mason v. Innes*[13] would have had to be considered. If the principles

[11] [1956] A C. 58.
[12] (1964) 41 T C. 389
[13] [1967] 1 Ch. 1079.

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applied in such cases apply to matters arising under the Canadian *Income Tax Act,* it would appear, strangely enough, that the result would depend on whether the taxpayer kept his accounts on a cash or accrual basis.

If he kept his accounts on a cash basis, he would not bring in any amount on the revenue side of the accounts of the business in respect of the stock-in-trade removed from the business even though the cost of acquiring it was reflected in the accounts of the business. If he kept his accounts on an accrual basis, he would bring in, as revenue, the value of the stock-in-trade so removed as that value was at the time of removal.

I express no opinion as to the principles applicable in similar cases under the Canadian statute. (See *Frankel Corpn. Ltd. v. M.N.R.*[14] for a limitation on the application of the English cases.) I merely make the comment that, if the English cases apply, it would appear that, if the appellants, who have been assessed without complaint on the basis that they kept their accounts on an accrual basis, had taken the options out of their business and given them to Adrien Lagacé Inc., or used them for some purpose that had nothing to do with their business (e.g., to pay off the debt of Adrien Lagacé Inc. to the Bank pursuant to their contract with Fortin), they would have had to bring into their business revenues the value of the options as of that time, which would have been, I should have thought, more or less the amount of the profit that was made by the immediate turning of the options to account.

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[14] [1959] S.C.R. 713.

BETWEEN:

Vancouver 1968

March 7-9

March 20

JOHN S. DAVIDSON ....APPELLANT;

AND

THE MINISTER OF NATIONAL REVENUE ....} RESPONDENT.

Income tax—Capital or income—Private company formed to finance building companies—Shares received from building companies as compensation—Conversion to public company—Sale of shareholders' shares—Whether shareholders' profit taxable.

Appellant, an insurance broker, and five other men were the sole shareholders and directors of the W company, a private company incorporated in British Columbia in 1954 which advanced money to a number of corporations each of which was set up by W company's directors to construct an apartment block or commercial building. The separate companies obtained some of their funds from the W company which in turn borrowed money from a bank on its shareholders' guarantees. As consideration for the loans the W company received 10% of the shares of each of the separate companies. Such shares were intended to pay an 8% annual dividend. By December 1958 the W company had received nearly 462,000 shares in 19 separate companies and had received dividends from such shares though no dividends were paid by the W company to its own shareholders. In October 1958 one of W company's shareholders died and because of ensuing difficulties in carrying on the above arrangement the W company was converted to a public company and its shareholders' shares sold. Appellant was assessed to income tax on the proceeds of the sale of his shares in W company, *viz* $67,546.

Held, in selling his shares appellant was realizing an investment and the gain thereon was not subject to income tax. Appellant did not acquire the shares with the intention of selling them at a profit and hence they did not become inventory in a business.

Irrigation Industries Ltd. v. M.N.R. [1962] S.C.R. 346; *Moluch v. M.N.R.* [1967] 2 Ex. C.R. 158; [1966] C.T.C. 712; *M.N.R. v. Firestone Management Ltd.* [1967] 1 Ex. C.R. 340; [1966] C.T.C. 771, referred to.

INCOME TAX APPEAL.

P. N. Thorsteinsson for appellant.

T. E. Jackson and *S. A. Hynes* for respondent.

SHEPPARD D.J.:—The appellant, John S. Davidson, contends that the sum of $67,546.74 received in 1959 from the sale of shares in Combined Estates Ltd. (formerly Welfar Holdings Ltd.) was capital, and the Minister was in error in including that amount in the appellant's taxable income. On the other hand, the Minister contends that the sum was taxable income. That is the issue. The facts follow.

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In 1935 the appellant moved from Calgary, Alberta, his birth place, to Vancouver, B.C. From 1936 to 1938 he was employed by H. A. Roberts Ltd. of Vancouver in their real estate business. In 1938 he joined Parsons, Brown Ltd., Vancouver, to sell insurance and apart from being in the army has since been engaged in insurance, formerly in selling for an agent, latterly as insurance broker. During the war he was in the army and in 1946 he rejoined Parsons, Brown Ltd. managing their sales agency. Later he was associated with R. M. Abernathy (Alberta) Ltd. and Abernathy Insurance Associates Ltd., Vancouver, with B. L. Johnson Walton (Alberta) Ltd. and B. L. Johnson Walton Co. Ltd. That is, the appellant was associated for some years with the Abernathy Companies of which he was a member and they subsequently combined with the Johnson Walton Companies. In 1959 Johnson Walton Companies merged with Reid, Shaw & McNaught, insurance brokers, and the appellant has since continued as a partner of that firm.

On 10th December, 1954 Welfar Holdings Ltd. (later Combined Estates Ltd.) and also B. C. Estates Ltd. were incorporated. The appellant was acquainted with all of those who became shareholders and directors other than Whitelaw and was approached to join the Company (Welfar) by Donald Farris. Welfar Holdings Ltd. was incorporated as a private company with the objects in the Memorandum of Association (Ex. A-1, Item 21); the initial shareholders were Donald Farris, the appellant, Ralph K. Farris, Frank S. Welters and James S. McKee, each holding 200 shares purchased at a dollar per share. B.C. Estates Ltd. was incorporated with the same shareholders holding the same number of common shares, and in addition, preference shares to the amount of $4,600, and was formed to purchase shares in other companies and to resell to the public. In March, 1956 each of the five shareholders issued 20 shares to Geoffrey H. Whitelaw in each of the companies at the original subscription price of one dollar per share.

The business of the two companies, Welfar and B.C. Estates, was to finance each of other companies called "little companies" to build an apartment block or commercial building in Vancouver, and the business was carried out as follows: Whitelaw would select a property suitable for building and if approved by the directors of Welfar, a little company would be formed to purchase the property and to build thereon an apartment block or commercial building. The little company would obtain the funds, by mortgage of the property, and the balance by borrowing from Welfar on promissory note. That balance was borrowed by Welfar from a bank on the guarantee of each of the six directors and then lent by Welfar to the little company for which loan Welfar would receive 10% of the shares in the little company (Ex. A-2, para. 5). Thereupon the little company would enter into an underwriting agreement to sell B.C. Estates Ltd. its shares at 85 or 90 cents. The shares of the little company were then sold by B.C. Estates Ltd. at par ($1.00) and the monies received by the little company would be used to repay the advance from Welfar. The shares of the little company were made saleable by the prospect of receiving 8% in dividends; typical prospectuses are Exhibit A-1, Items 6, 7 and 8. Welfar had with the bank an authorized credit of $165,000 of which $146,000 was the most outstanding, and on 20th October, 1958 the bank loan was $115,000. Those represented loans to little companies and each director of Welfar was liable to the bank jointly and severally.

As the result of this plan, by December, 1958 Welfar had received 461,912 shares in 19 little companies which shares were placed in escrow by the Registrar of Companies (Ex. A-2, Supplementary Agreement, p. 3), and Welfar received dividends from the little companies to the amount appearing in Exhibit A-1, Items 1 and 2, but Welfar had paid no dividends to its shareholders. At no time were any of the shares in Welfar or in any of the little companies listed, and all the little company shares were sold through B.C. Estates Ltd., of which the shareholders were those in Welfar.

On 21st October, 1958, James S. McKee, one of the shareholders of Welfar and B.C. Estates, died, and this death resulted in difficulty in proceeding with the plan of Welfar as it involved Welfar borrowing from the bank on the guarantee of the five directors. The estate of McKee wished to liquidate the assets, and the surviving directors, including the appellant, were not prepared to guarantee the loans and so carry the estate. As a result, the outstand-

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ing shares in Welfar, which were owned respectively by the estate of McKee and the other five (including therein Whitelaw) were sold through B.C. Estates Ltd. as follows:

22nd December, 1958—9,000 unissued shares in Welfar were cancelled and the 1,000 shares issued were divided into 420,000 shares at a nominal or par value (Ex. A-1, Item 9) and the Registrar of Companies authorized the issuing of 420,000 shares at a nominal or par value (Ex. A-1, Item 11);

15th January, 1959—Welfar's name was changed to Combined Estates Ltd. (Ex. A-1, Item 12);

26th January, 1959—Combined Estates Ltd. converted itself from a private company into a public company (Ex. A-1, Item 13). Thereupon the shareholders in Combined Estates Ltd. sold their shares to B.C. Estates Ltd. (Ex. A-1, Item 17) and B.C. Estates Ltd. sold them to the public, and from the proceeds of the sale the share of the appellant amounting to $67,546.74 was assessed by the Minister as taxable income.

Following the sale the five surviving directors, the appellant and four others, including Whitelaw, incorporated Farwel Holdings Ltd. for the purpose of continuing the same plan which had been followed by Welfar (Ex. A-2, Supplementary Agreement, para. 5) and Farwel thereupon, according to the plan, financed three little companies to build three buildings. It was learned that the price of lots had increased to such an extent that it was necessary to build highrise apartments to produce a return of 8% on the investment, but the building of the highrise apartments increased the loan from the bank and the amount to be guaranteed by the directors; as a result, Farwel did not continue financing other little companies.

The issue results in the ultimate question whether the shares of the appellant in Welfar were an investment and the proceeds capital, as the appellant contends, or whether the shares were inventory in a business of the appellant and therefore the profit taxable income as the Minister contends.

The appellant has testified that the shares in Welfar were an investment, that his business was selling insurance and the proceeds from the shares were the realizing of an investment and therefore capital. His testimony is:

(a) that his business throughout was insurance, commencing with Parsons, Brown, and through other associations until 1959 when he joined Reid, Shaw & McNaught, therefore throughout he was selling insurance, latterly as insurance broker;

(b) that the shares in Welfar were an investment as they were bought for dividends. No dividends were declared by Welfar. However it did receive dividends at the rate of 8% from the various little companies in each of which it held 10% of the shares (Ex. A-1, Items 1 and 2). It is immaterial that Welfar paid no dividends as its shares were capable of producing dividends: *M.N.R. v. Valclair Investment Company Limited*[1]; and that the shares were purchased for the income which they could produce and were therefore an investment;

(c) that the sale was caused by the death of McKee on the 21st October, 1958, that is, by the desire of the personal representatives to administer the estate and the reluctance of the surviving directors to become personally liable under the guarantee for the benefit of the estate.

The death of McKee produced reasons for not continuing the former plan to a degree more substantial than the appellant had considered. The death of McKee caused the continuing directors to lose a right of contribution against McKee as a continuing director—and raised the question whether the estate or the personal representative would be liable to the bank for future advances on previous guarantees, which would depend on when the bank had notice of the death (18 *Halsbury* (3rd Ed.) p. 526, para. 869), and the further question whether there was any right of contribution against the estate for any future advance (*Labouchere v. Tupper*)[2]. Moreover, in continuing with a legal representative there is always the potential liability for knowingly participating with the legal representa-

[1] [1964] Ex. C.R. 466; [1964] C.T.C. 22.

[2] (1857) 11 Moo. P.C. 198 at p. 211; 14 E.R. 670 at p. 679.

tive in a breach of trust: *Barnes v. Addy*[3] and *Keeton on Trusts* (8th Ed.) p. 850. Hence the death of McKee was an adequate reason for not continuing with the initial plan.

On the appellant's evidence, the shares in Welfar were bought to be held for their income and not for resale and that is corroborated by the fact that Welfar Holdings Ltd. was a private company and under the *Companies Act*, R.S.B.C. 1948, c. 58, sec. 2, continued in 1960, c. 67, sec. 2, a private company means a company that by its memorandum or articles:

(a) restricts the right to transfer its shares, and

(b) limits the number of its members to 50 or less (other than employees, actual or past), and

(c) prohibits any invitation to the public to subscribe for any shares or debentures of the company.

It is not contended that it was impossible for the appellant to have sold his shares in a private company, but the right to transfer the shares was restricted. What that restriction was we do not know, as the memorandum only was produced, but a private company may be popularly regarded as equivalent to an incorporated partnership; that is, a transferee is admitted at the discretion of the continuing members. In any event, Welfar was not initially a public company and therefore the shares were not of a nature to be offered generally to the public. After deciding upon the sale of the shares, Welfar was turned into a public company in order to avoid the restrictions imposed upon a private company. That sale was merely a means of realizing on an investment: *M.N.R. v. Firestone Management Limited*[4], and the proceeds from the sale to B.C. Estates Ltd., being proceeds of an investment would be likewise capital: *Frankel Corporation Ltd. v. M.N.R.*[5]

On that evidence the shares were an investment and hence a capital asset; that, of course, is subject to other evidence establishing that the proceeds should be treated as taxable income. The Minister contends that the profit of the shares is taxable income within sections 3 and 4, being

[3] [1874] L R. 9 Ch. A. 244.

[4] [1967] 1 Ex.C R. 340; [1966] C.T.C. 771.

[5] [1959] S.C R. 713; [1959] C.T.C. 244.

profit derived from a business within section 139(1)(*e*), which extends "business" to include "an adventure...in the nature of trade".

To prove taxable income it is not enough in particular instances to prove a business, in that a business does not preclude there being capital assets, such as the building premises of a department store or of a brokerage company, and the proceeds of which in general will not be taxable income. In some instances the proof of a business within Section 139(1)(*e*) is sufficient to prove an inventory by reason of the implied intent of the taxpayer or by reason of the nature of the property. Two positive tests of carrying on business are set out in *Irrigation Industries Ltd. v. M.N.R.*[6] (cited for the Minister) where Martland J. stated at p. 352:

> The positive tests to which he refers as being derived from the decided cases as indicative of an adventure in the nature of trade are: (1) Whether the person dealt with the property purchased by him in the same way as a dealer would ordinarily do and (2) whether the nature and quantity of the subject-matter of the transaction may exclude the possibility that its sale was the realization of an investment, or otherwise of a capital nature, or that it could have been disposed of otherwise than as a trade transaction.
>
> I will deal first with the second of these tests, which, if applied to the circumstances of the present case, would not, in my opinion, indicate that there had been an adventure in the nature of trade.
>
> The nature of the property in question here is shares issued from the treasury of a corporation and we have not been referred to any reported case in which profit from one isolated purchase and sale of shares, by a person not engaged in the business of trading in securities, has been claimed to be taxable.
>
> Cases in which the nature and quantity of the property purchased and sold have indicated an adventure in the nature of trade include *The Commissioners of Inland Revenue v. Livingston* ((1926), 11 Tax Cas. 538) (a cargo vessel); *Rutledge v. The Commissioners of Inland Revenue* (1929), 14 Tax Cas. 490) (a large quantity of toilet paper); *Lindsay v. The Commissioners of Inland Revenue* ((1932), 18 Tax Cas. 43) and *Commissioners of Inland Revenue v. Fraser* ((1942), 24 Tax Cas. 498) (a large quantity of whisky); *Edwards v. Bairstow* ([1956] A.C. 14) (a complete spinning plant) and *Regal Heights Ltd. v. Minister of National Revenue* ([1960] S.C.R. 902) (40 acres of vacant city land).
>
> Corporate shares are in a different position because they constitute something the purchase of which is, in itself, an investment. They are not, in themselves, articles of commerce, but represent an interest in a corporation which is itself created for the purpose of doing business. Their acquisition is a well-recognized method of investing capital in a business enterprise.

[6] [1962] S.C.R. 346

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and at p. 353:

> Furthermore, the quantity of shares purchased by the appellant in the present case would not, in my opinion, be indicative of an adventure in the nature of trade, as it constituted only 4,000 out of a total issue of 500,000 shares.

The first test set out in *Irrigation Industries Ltd. v. M.N.R.* is dealt with in *M.N.R. v. Taylor*[7], where the subject matter was 1,500 tons or 22 carloads of lead, and its kind and quantity implied an intent to sell to the employer. For the second test, cases are referred to in *Irrigation Industries Ltd. v. M.N.R.*

It would appear that when either test is applicable then the subject matter is denoted as inventory. Hence, if a person bought property with the intention of selling at a profit then he has dealt in general with it in the same way as a trader and impliedly has treated it as inventory by intending to make a profit by the purchase and sale. On the other hand, as stated in the *Irrigation* case at p. 352: "Corporate shares are in a different position because they constitute something the purchase of which is, in itself, an investment."

Therefore these tests do not apply to shares as they may be an investment, and to make the proceeds of shares taxable income the circumstances must indicate:

(1) That there was a business within section 139(1)(*e*);

(2) That the shares were properly treated as inventory in the business.

An instance of the converting of capital to inventory appears in *Moluch v. M.N.R.*[8] where the taxpayer bought farmland which was used initially for his home and as a farm and therefore was a capital asset, but later was subdivided to be sold for building lots. There Cattanach J. said:[9]

> If, at some subsequent point in time, the appellant embarked upon a business using the lands as *inventory* in the business of land subdividing for profit, then clearly the resultant profits would not be merely the realization of an enhancement in value, but rather profits from a business and so assessable to income tax in accordance with Sections 3 and 4 of the *Income Tax Act*, R.S.C. 1952, chapter 148.

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[7] [1956-60] Ex.C R. 3.

[8] [1967] 2 Ex. C.R. 158; [1966] C.T.C. 712.

[9] [1967] 2 Ex. C.R. at p. 165; [1966] C.T.C. at p. 718.

That judgment was approved in *M.N.R. v. Firestone Management Limited* (*supra*), by Jackett P.[10] Hence the profits in the proceeds of the appellant's shares in Welfar are taxable income only if there was a business in which such shares were inventory.

The Minister contends that the profits are taxable income for the following reasons:

(1) That the plan of business adopted by Welfar, B.C. Estates and the little companies and adopted by the appellant and other directors by giving guarantees was of a complex and detailed nature which could be nothing but a business by the appellant and whoever entered into it. Exhibit 2-A, para. 5 shows the complex working out of the plan through the companies, Welfar, B.C. Estates Ltd. and the little companies, which resulted in Welfar obtaining 10% of the outstanding shares in the 19 companies referred to in Exhibit A-2 (Supplementary Agreement, p. 3), and in B.C. Estates Ltd. receiving a commission on the shares sold to the public and later a fee for managing the properties of the little companies.

It is not a question whether Welfar and associated companies were in business: that is evident, but the appellant being a shareholder: *Macaura v. Northern Assurance Company Limited*[11], or a director: *Parker v. McKenna*[12], would give him no proprietary interest in the companies' business. The question here is whether the appellant in purchasing his shares from Welfar, did so in the business of buying and selling such shares so as to make them an inventory. That is excluded by the fact that Welfar was a private company; the evidence is rather consistent with such shares being an investment.

(2) That such a promotion of Welfar must give rise to income receipts by the appellant, for the following reasons:

(a) The appellant was a partner in a stockbrokerage firm, Locke, Grey & Co., 1958, and he received

[10] [1967] 1 Ex C.R. at p. 345; [1966] C.T.C. at pp 774-5.
[11] [1925] A.C. 619
[12] (1875) 10 Ch. App. 96

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therefrom net profits of $3,851.97 (Ex. R-1), therefore his purchasing shares from Welfar was the mere continuing of his operations as broker. That does not follow. The appellant was a silent partner and took no active part in the management. As partner, though silent, he had an interest in any shares purchased by that firm because such purchase would be a joint purchase on behalf of all the partners. His shares in Welfar were not purchased by or for Locke, Grey & Co., nor was it a joint purchase, but a several purchase by the appellant for himself. That was not "an adventure... in the nature of trade" for the reasons given in *Irrigation Industries Ltd. v. M.N.R.* (*supra*).

(b) The appellant made money in companies engaged in many lines of business, therefore the variety of companies in which he was interested indicated that he was engaged in this instance in a further business (Ex. A-1, Item 16). On the other hand, throughout, the appellant has continued in the business of selling insurance and the amount he would have for investment would be derived from his profits in selling insurance and also the profits derived from investments. The number of investments does not exclude their being capital investments. Also there is no evidence that the quantity of shares held by the appellant gave him the control of any of those other companies. The absence of such control did indicate there was no adventure in the nature of trade and there was an investment in *Irrigation Industries Ltd. v. M.N.R.* (*supra*), at p. 353, and the fact that active control was exercised was considered relevant in *Mainwaring v. M.N.R.*[13] and *Robertson v. M.N.R.*[14]. In any event, we are not here concerned with the nature of the appellant's interests in other companies but with the nature of his

[13] [1965] 1 Ex.C.R. 271; 64 DTC 5214.

[14] [1964] Ex.C.R. 444; 63 DTC 1367; (affirmed 64 DTC 5113).

interest in his shares in Welfar, a private company, which were presumably not purchased for the purpose of resale and were not inventory.

(3) That the appellant in joining Welfar has become associated with persons in the business of buying and selling shares and therefore, because of his association, he must be known as a person who is so engaged in buying and selling shares. As a partner in Locke, Grey & Co. he was undoubtedly interested in those purchases made by the firm on behalf of the firm, but in this instance it was not a joint purchase but a several purchase by the appellant for himself and he is not concerned with the motives in which other members may have purchased their shares, whether with an "alternative intention" as in *Regal Heights Ltd. v. M.N.R.*[15], or even with a multiple of intentions.

The minister has cited the following additional cases which are distinguishable on the facts. In each case it was held that the transaction was part of a business and invariably that the subject matter was purchased for the purpose of the taxpayer selling at a profit.

In two cases the shares were bought for the purpose of selling at a profit and the control and management indicated a business to promote the value of the shares: *Mainwaring v. M.N.R., (supra); Robertson v. M.N.R.* (*supra*). On the other hand, in *Gladys Mainwaring v. M.N.R.*[16], it was held that her purchase of shares was not part of a business and presumably not part of the business of her husband.

In other instances, the taxpayer had a business for dealing in the subject matter and he was held to have purchased and sold the subject matter as a continuation of that business: *Whittall v. M.N.R.*[17]; *Gairdner Securities Ltd. v. M.N.R.*[18]; *McMahon and Burns Limited v. M.N.R.*[19]; *Stuyvesant-North Limited v. M.N.R.*[20]; *Ritchie v. M.N.R.*[21]; *Osler, Hammond & Nanton Ltd. v. M.N.R.*[22].

15 [1960] S C R 902
16 63 DTC 1029.
17 [1965] 1 Ex C R. 342; 64 DTC 5266; 67 DTC 5264.
18 [1952] Ex C R. 448.
19 56 DTC 1092.
20 [1958] Ex C.R. 230; 58 DTC 1092.
21 60 DTC 595.
22 [1963] S.C.R. 432; 61 DTC 595; 63 DTC 1119.

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In *Morrison v. M.N.R.*[23], the subject matter was grain purchased for resale at a profit by one who was in the business of buying and selling grain.

In *M.N.R. v. Spencer*[24], the acquiring by a solicitor of mortgages was held to be so close to the normal practice of a solicitor as to be part thereof and therefore the profits were taxable income under Sections 3 and 4.

Land purchased to be sold for one purpose and sold for another was held to be included in the business by reason of the doctrine of frustration and the rule of alternative intentions and hence the profit was taxable income: *Regal Heights Ltd. v. M.N.R., (supra); Rothenberg v. M.N.R.*[25], *Slater et al. v. M.N.R.*[26]; *Diamond v. M.N.R.*[27]; *Farris v. M.N.R.*[28]

In *Mikula v. M.N.R.*[29], the appellant a nurse, was in partnership with her brother who purchased for the firm for the purpose of selling for a profit, and which she, as a partner, was held to have acquired as part of that business and was therefore taxable on the income.

In *Campbell v. M.N.R.*[30], the sale of shares in a private company was held to be merely a means of selling the apartment building which the company and also the taxpayer were in the business of constructing.

Basically those cases depend on a finding of fact, in effect, that the taxpayer acquired the subject matter with the intent of selling at a profit. Whether or not that intent existed was a question of fact, and on that finding, depended the conclusion in law that the profit was derived from inventory, and therefore was taxable income.

That distinguishes the case at bar as here the initial intention of the appellant was to hold the shares in the private company, Welfar, to produce dividends and there was no intent to sell until that intent was necessitated by the subsequent death of McKee.

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23 [1928] Ex.C R. 75; (1927) 1 DTC 113.

24 61 DTC 1079 at p. 1092.

25 [1965] 1 Ex.C R. 849; 65 DTC 5001.

26 [1966] Ex.C R. 387; 66 DTC 5047; [1966] CTC 53.

27 [1967] 1 Ex C R. 541; 66 DTC 5434.

28 63 DTC 1221.

29 66 DTC 636.

30 [1953] 1 S.C R. 3; 52 DTC 1187.

On the 21st October, 1958, the death of McKee occurred and that fortuitous event resulted for the first time, so far as the appellant was concerned, in deciding not to continue the association but to sell his shares in the company, and the subsequent steps were consistent with realizing on an investment; namely, the converting to a public company so that the shares could be sold unfettered, and the subdividing of the shares into their approximate book value so that the full value could be received.

The evidence therefore does not establish that the appellant: (1) entered into the business of dealing in those shares, (2) nor that such shares became an inventory in such business. The realizing of a profit on the shares as an investment is immaterial: *Irrigation Industries Ltd. v. M.N.R.* (*supra*), at pp. 350 and 354-5, citing *Californian Copper Syndicate v. Harris*[31].

In the result the appeal is allowed with costs to the appellant. The assessment by the Minister is vacated and the matter referred back for reassessment in accordance with:—

(a) The agreement (Ex. A-3) that $7,485, being 50% of the amount of $14,970 received from Western Technical Consultants be included in the income;

(b) That the sum of $67,546.74, the amount here in question, be considered as capital and not as taxable income.

[31] (1904) 5 T.C 159.

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BETWEEN:

VAUGHAN CONSTRUCTION COMPANY LIMITED .... APPELLANT;

AND

THE MINISTER OF NATIONAL REVENUE .... RESPONDENT.

AND BETWEEN:

THE MINISTER OF NATIONAL REVENUE .... APPELLANT;

AND

VAUGHAN CONSTRUCTION COMPANY LIMITED .... RESPONDENT.

Income tax—Disposition of land by company—Expropriation of land—Whether profit of business—Award of partial compensation for expropriation—Income of what year—Amount receivable—Income Tax Act, s. 85B(1)(b).

In 1953 appellant company, which had previously carried on a construction business and sold fill, acquired 12.3 acres of undeveloped land in Halifax for $67,900. In 1954 after rejecting an offer of $130,750 appellant exchanged the 12.3 acres for 2.9 acres in a commercial area of Halifax plus $33,000 and as a condition of the transaction covenanted to convey the property to the city on request for $87,520 if it failed to erect an office building thereon which would be subject to city taxes. In August 1955 while appellant was engaged in demolishing some old buildings on the property the Province expropriated the land. In June 1957 an arbitrator fixed compensation for the 2.9 acres at $280,000 plus interest and ordered the Province to pay appellant on account $87,520 plus certain interest, and the Province did so forthwith. In 1961 the Supreme Court of Canada on appeal allocated the compensation $96,240 to Halifax and the remainder to appellant.

Held, (1) The profit made on the exchange of the 12.3 acres in 1954 and on the expropriation of the 2 9 acres in August 1955 was in each case a business profit and chargeable to income tax. On the evidence appellant acquired both properties as speculations with a view to profiting on their disposition. *Taylor v. M.N.R.* [1956-60] Ex.C.R. 3 and *Irrigation Industries Ltd v. M.N.R.* [1962] S.C.R. 346, applied.

(2) The $87,520 plus interest paid appellant in June 1957 on the arbitrator's award was attributable to appellant's 1957 taxation year. While compensation for expropriated property is not to be taken into account by a taxpayer who computes income on the accrual basis until the amount is fixed by arbitration or agreement appellant became immediately entitled to the amount awarded by the arbitrator in June 1957 and such amount was therefore to be taken into account as an amount receivable in that year. *M N.R. v. Benaby Realties Ltd.* [1968] S.C.R. 12; [1967] C.T.C. 418, applied and distinguished.

INCOME TAX APPEALS.

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VAUGHAN CONSTRUCTION CO. LTD. v. MINISTER OF NATIONAL REVENUE AND MINISTER OF NATIONAL REVENUE v. VAUGHAN CONSTRUCTION CO. LTD.

H. B. Rhude and *D. R. Chipman* for Vaughan Construction Company Limited.

I. M. MacKeigan, Q.C. and *M. J. Bonner* for Minister of National Revenue.

THURLOW J.:—These appeals are from judgments[1] of the Tax Appeal Board which dismissed the taxpayer's appeal from a re-assessment of income tax for the year 1954 and allowed its appeal from a re-assessment of tax for the year 1957. In each case there is an issue as to whether profit realized in a particular transaction was profit from a business as defined in the *Income Tax Act* and therefore taxable as income under its provisions. With respect to the 1957 re-assessment there is also an issue as to whether, if taxable at all as income, the profit in question was taxable as income of that year.

The appeals were heard together on common evidence which consisted of (1) oral testimony by Mr. Harry Gordon an accountant who since 1956 has prepared the appellant company's financial statements, Dr. A. Murray MacKay, the Chairman of the Board of Directors of the Maritime Telegraph and Telephone Company Limited, Mr. Angus P. Gladwin, a claims agent in the employ of the Province of Nova Scotia and Mr. Kenneth S. Mahon, a trust officer in the employ of the Canada Permanent Trust Company, (2) a number of documents which were admitted by consent and (3) portions of the examination for discovery, conducted on behalf of the Minister, of Bernard J. Vaughan who at all material times was the President and Managing Director of the appellant company and the owner of its issued capital stock. Mr. Vaughan, however, was not called as a witness at the trial.

The appellant company was incorporated under the *Companies Act* of Nova Scotia in 1943 with broadly expressed objects and powers including those of acquiring the plant and machinery of Bernard J. Vaughan doing business as a general contractor and of carrying on various businesses including dealing in real property. Thereafter for three or four years it carried on a construction business

[1] (1965) 39 Tax ABC 380.

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in which it constructed dwelling houses in what was referred to as the Vaughan subdivision in the northern part of the City of Halifax. This business came to an end by 1948 and from that time until the events which occurred in 1953 and subsequently the company's business activities seem to have consisted in selling fill which it obtained from a block of properties in an industrial zone on Kempt Road in the City of Halifax which Bernard J. Vaughan had in the meantime acquired.

In his personal capacity Vaughan was a trader in real estate. He acquired, subdivided and sold the property referred to as the Vaughan subdivision and he acquired, consolidated and sold in pieces the industrial land on Kempt Road already mentioned. He was also engaged in a venture in acquiring properties on what was referred to as the airport highway, which did not turn out satisfactorily, and he owned a company known as Airway Broadcasting Company which acquired property in what is known as Geizer's Hill in the County of Halifax a portion of which was later sold at an enhanced price to the Public Service Commission of Halifax following a threat of expropriation by that body.

In 1950 Vaughan, a Mr. Doyle and a Mr. Cousins became engaged in a transaction in which Messrs. Doyle and Cousins provided the financing for and purchased a 12.3 acre property on Howe Avenue in the northern part of the City of Halifax. This was undeveloped land a portion of which was rocky and some of which was swamp. The plan was to make profit by the sale of the property and Vaughan was to advise and assist in disposing of it. He was to be entitled to a half interest in the property and to half of the proceeds therefrom after Messrs. Doyle and Cousins had recovered their initial investment.

In 1951 and 1952 the appellant company supplied fill for this property for the account of Doyle and Cousins to the value of $27,900 but none of the property had been sold when Mr. Cousins died and his executors and Doyle proposed putting the property up for sale. Vaughan thereupon arranged to borrow $40,000 and purchased the property for the appellant company for that amount plus the indebtedness for the fill. The transaction was completed in September 1953 but the offer to purchase had been made some months earlier and not later than May 12, 1953, when a deposit of $4,000 was paid to the Canada Permanent Trust Company which held the title as trustee and represented Mr. Doyle and the executors of Mr. Cousins' estate.

Some years earlier the Maritime Telegraph and Telephone Company had acquired from the City of Halifax for $87,520 a 2.9 acre property in downtown Halifax on the corner of Spring Garden Road and Queen Street known as the Bellevue property which it had intended to use in part as a site for a head office building and in part as a service area. As part of the purchase transaction the company had obligated itself to construct a first class office building on the land and if it failed to do so to reconvey the land to the city upon request for $87,520. The company, however, ultimately came to the conclusion that this property was not suitable for its purposes and in 1953 began looking for another more suitable property in the course of which by a letter dated June 10, 1953, which followed verbal discussions with Mr. Vaughan, it offered him 25¢ per square foot for the Howe Street property. This offer, which would have amounted to some $130,750 for the property, was declined not, ostensibly, because it was not high enough but because Vaughan was unwilling to sell. He suggested another property in which he was not interested and an offer was made by the Maritime Telegraph and Telephone Company for it which was also declined by the owner. In the following year discussions again took place between representatives of the Maritime Telegraph and Telephone Company and Mr. Vaughan with a view to that company acquiring the Howe Street property in the course of which Mr. Vaughan suggested that while he did not want to sell he would trade that property for the Bellevue property providing the conditions were satisfactory. Eventually, following arrangements with the city, a transaction was completed in which the appellant company transferred the Howe Street property to the Maritime Telegraph and Telephone Company in exchange for the Bellevue property and $33,000 and as part of the transaction the appellant company covenanted with the City of Halifax to construct a first class office building on the Bellevue property as soon as practicable, to reconvey the property to the city on request for $87,520 if it failed to proceed with construction of the building and that the building when constructed

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would be subject to taxation under the provisions of the Halifax City Charter. From the point of view of the city this was important since there was an infirmary to the southward of the property and property of the province to the eastward and if either became owner of the property it might be exempted from city taxation. From the point of view of the appellant company it represented a restriction upon its rights in the property.

In the meantime while in possession of the Howe Street property the appellant company had received a sum of some $8,900 from the city on the purchase of a sewer easement across it.

In assessing the appellant company for 1954 the Minister added to its declared income the $8,900 so received, the $33,000 received from the Maritime Telegraph and Telephone Company and the value of the Bellevue property at $87,520 which amounts, after deducting the cost of the Howe Street property, left a profit upon which tax was assessed. It is the liability of the appellant company for tax on this profit that is in issue in the 1954 appeal.

After obtaining title to the Bellevue property the appellant began demolition of a number of old buildings thereon and had discussions with a number of persons interested in acquiring the property or portions of it but the demolitions had not yet been completed when in August 1955 the Province of Nova Scotia expropriated the property. Vaughan had been informed as early as February 1955 of the province's interest in acquiring the property and discussions had taken place respecting a price in the month preceding the expropriation but no agreement had been reached. By an order dated June 4, 1957 made by His Honour Judge Pottier, Judge of the County Court for District Number One (as he then was), acting as an arbitrator, the compensation payable in respect of the property was fixed at $280,000 plus 5% thereof for compulsory taking and it was further ordered that, pending further decision or order as to the balance of the said compensation payable, the province should pay to the appellant company $87,520 "on account of the said compensation together with five per centum (5%) thereof by way of allowance for compulsory taking, making a total of ninety-one thousand eight hundred and ninety six dollars ($91,896)" together with interest thereon at 5% per annum from the 19th of June, 1956 until payment. By the same order leave was reserved to any of the parties to apply from time to time with regard to the balance remaining of the said compensation. In a decision filed prior to the making of the order the learned Judge had expressed the opinion that there could be no question regarding the rights of the appellant company to the sum of $87,520 of the $280,000 compensation which he had previously assessed, and he had intimated that he would grant an order for payment of $87,520 to the appellant company together with proportionate interest and allowance for compulsory taking.

No appeal was taken from this order either by the City of Halifax or by the Province of Nova Scotia, which had been ordered to make the payment, and the province in fact paid the appellant company the sum so ordered on June 13, 1957. The Minister included the amount so received in computing the appellant's income for tax purposes for the year 1957 and it is the correctness of his so doing that is in issue in the 1957 appeal.

It should be added that in 1959 a further order with respect to the remainder of the compensation money was made and was the subject of appeals by both the City of Halifax and the Vaughan Construction Company Limited to the Supreme Court of Nova Scotia *in banco* and later by the City of Halifax to the Supreme Court of Canada where it was ultimately determined that the City of Halifax was entitled to $96,240 of the $280,000 award of compensation and the appellant company to $183,760 thereof in each case with interest thereof at 5% per annum from June 18, 1956, to the date of payment. The formal judgment of the Supreme Court of Canada contained no reference to the 5% allowance for compulsory taking referred to in the order of June 4, 1957 and in the order from which the appeal to the Supreme Court was taken but the reasons for judgment[2] which are referred to in the reply and to which my attention was invited in the course of argument by counsel for the Minister clearly show that the 5% for compulsory taking was disallowed by the Supreme Court of Canada.

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[2] *Vide Regal Heights Limited v. Minister of National Revenue* [1960] S.C.R. 902 at 907.

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In the view I take the profit realized by the appellant company from its acquisition and disposal of the Howe Street property was plainly profit from a venture in the nature of trade and thus from a business as defined in the *Income Tax Act*. Apart from the fact that the first offer made by the Maritime Telegraph and Telephone Company was turned down, which is explained only by the statement made by Mr. Vaughan on discovery that he was exploring several possibilities for development of the property either for residential or industrial purposes, nothing in the evidence even suggests that the appellant acquired the property otherwise than as a speculation in undeveloped real estate. Mr. Vaughan when first acquiring an interest in it by entering into the transaction with Messrs. Doyle and Cousins did so in the course of a scheme for making profit by disposing of it and there is nothing to indicate that this purpose for it ever changed or that the intention of his company was in any way different from his own. The company did nothing with the property in the time it held it save to arrange a price for the easement acquired by the city and to dispose of it in the transaction with the Maritime Telegraph and Telephone Company and while there is evidence that Mr. Vaughan enquired of an insurance company if financing could be obtained for the construction of apartment buildings on it and was told that it would not, such evidence falls far short of establishing that the appellant company had plans for constructing such buildings. Even less does it establish that the appellant company planned to construct such buildings to be held as investments. Moreover in the hands of such a company the property itself consisting as it did of some 12.3 acres of undeveloped and unproductive land zoned for industrial purposes has the character and appearance of inventory rather than of a fixed or capital asset.

Finally the property was dealt with by the appellant company in the same way that a speculative dealer in land might be expected to deal with it; acquiring it, holding it for a comparatively short time, during which it served no purpose in the appellant company's hands, until an interested party came along and then making it the subject of a profitable trade for a substantial sum in cash and another valuable and readily saleable piece of property.

Both of the positive guides enunciated by the former President of this Court in *Taylor v. Minister of National Revenue*[3], which were cited with approval by the Supreme Court of Canada in *Irrigation Industries Limited v. Minister of National Revenue*[4], thus indicate that the transaction from which the profit here in question arose was an adventure in the nature of trade in addition to which the intention of Mr. Vaughan in acquiring an interest in the property and of his company in acquiring the property itself serve to confirm this conclusion.

The appeal in respect of the 1954 re-assessment accordingly fails.

I reach a similar conclusion with respect to the nature of the profit realized from the Bellevue property, though in this case since the property was expropriated there was no disposal transaction from which any conclusion can be drawn. That the property, like the one for which it was exchanged, was of an inventory nature in the appellant company's hands is, however, in my view, plain. Though different in character from the Howe Street property it too was a comparatively large area, large enough to accommodate a number of substantial commercial structures, and it was located in a commercial area in which there was a great demand for land. Moreover, apart from the fact that the company covenanted with the city to erect a first class office building on a part of the property which would be subject to municipal taxation, which is equivocal on the question to be determined, nothing in the evidence indicates that the company had any plans whatever to build on the property. Rather the contrary is indicated. In the period of nine months during which the appellant company held the title it neither developed plans for such a building, nor settled on specific ideas as to how to develop the property, nor did it employ anyone to formulate such ideas or to draw plans. It had no financial resources of its own with which to build a first class office building; yet it neither arranged for financing nor made efforts to secure tenants for such a building. There is even less evidence of any intention to hold the property, whether with or without a building thereon, as an investment. On discovery Mr.

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[3] [1956-60] Ex. C R 3

[4] [1962] S C.R. 346

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Vaughan said the plan for the property was simply to remove the old buildings and to explore the "possibility" of building an "A type" building, build it and leave the rest undeveloped for another day, and that the determination of what would happen to the rest of the property would come later. He also said that in talking with the manager of a trust company about the property he mentioned that a particular party was interested in the whole of the property but that if the trust company would offer $6 per square foot for the portion the trust company wanted he would endeavour to have that held out of the transaction. It was submitted that the particular party referred to was the province and that this occurred after Mr. Vaughan became aware that the property would be expropriated but even if this was the fact (though I do not think it is established) it appears to me to show the situation to be one of an experienced dealer carrying on a business of trading in land. These facts, in my view, indicate that the property was acquired simply as a speculation with a view to turning it to account for profit in any way that might present itself, including sale and, in fact, apart from the demolition of the old buildings the only activity of the appellant company with respect to the property in the time it held the title appears to have consisted in talking with various prospective purchasers of the whole or part of it. In my view therefor the profit realized by the appellant from the Bellevue property was also profit from a business within the meaning of section 139(1)(*e*) of the *Income Tax Act.*

I turn now to the contention that in any event profit from the Bellevue property was not realized in the appellant company's 1957 taxation year. In the appellant company's reply this point was based on the contention that the year in which the profit must be taken to have been realized was the year in which the expropriation occurred, that is to say, 1955, but in argument the point was based on the contention that the compensation to be paid to the appellant company, whose financial statements were compiled on an accrual basis, was not ascertained in the 1957 year since the company's entitlement to compensation for the property was not finally determined until 1961 when the judgment of the Supreme Court of Canada was rendered. The contention was based on the judgment of that

Court in *Minister of National Revenue v. Benaby Realties Limited*[5] which was rendered after the filing of the appellant company's reply.

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In the *Benaby* case Judson J., speaking for the Court said at page 419:

> The taxpayer conducted its business on the accrual basis under Section 85B(1)(*b*), which reads:
>
> 85B.(1) in computing the income of a taxpayer for a taxation year,
>
> (*b*) every amount receivable in respect of property sold or services rendered in the course of the business in the year shall be included notwithstanding that the amount is not receivable until a subsequent year unless the method adopted by the taxpayer for computing income from the business and accepted for the purposes of this Part does not require him to include any amount receivable in computing his income for a taxation year unless it has been received in the year.
>
> The Crown's argument is that the general rule under the *Income Tax Act* is that taxes are payable on income actually received by the taxpayer during the taxation period; that there is an exception in the case of trade receipts under Section 85B(1)(*b*), which include not only actual receipts but amounts which have become receivable in the year; that the taxpayer's profit from this expropriation did not form part of its income for the year 1954 because it was not received in that year and because it did not become an amount receivable in that year.
>
> In my opinion, the Minister's submission is sound. It is true that at the moment of expropriation the taxpayer acquired a right to receive compensation in place of the land but in the absence of a binding agreement between the parties or of a judgment fixing the compensation, the owner had no more than a right to claim compensation and there is nothing which can be taken into account as an amount receivable due to the expropriation.

He said further at page 421:

> My opinion is that the Canadian *Income Tax Act* requires that profits be taken into account or assessed in the year in which the amount is ascertained.
>
> *Try v. Johnson,* [1948] 1 All E.R. 532, is much closer to the point in issue here. The claim was for compensation under legislation which imposed restriction on "Ribbon Development". When the case reached the Court of Appeal, the amount of compensation was admitted to be a trade receipt. The argument in that Court was directed to the appropriate year of assessment. The judgment was that the right of the frontager to compensation under the *Ribbon Development Act* contained so many elements of uncertainty both as to the right itself and the quantum that it could not be regarded as a trade receipt for the purpose of ascertaining the appropriate year of assessment until the amount was fixed either by an arbitration award or by agreement.

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[5] [1968] S C R 12; [1967] C.T.C. 418 at 419.

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Under the Canadian *Expropriation Act*, there is no doubt or uncertainty as to the right to compensation, but I do adopt the principle that there could be no amount receivable under Section 85B(1)(*b*) until the amount was fixed either by arbitration or agreement.

The right to compensation under the *Expropriation Act* of the Province of Nova Scotia is I think the same and as the financial statement of the appellant company and its income tax returns for 1956 and subsequent years, and possibly for earlier years as well, were prepared on an accrual basis the principle adopted by the Supreme Court appears to me to apply. However, after the making of the order of the arbitrator in June 1957 and the making of the payment directed thereby by the party directed to make it, who did not appeal therefrom, I do not think it could any longer be said that the appellant company had "a mere right to compensation" or that there was nothing which could "be taken into account as an amount receivable due to the expropriation". What up to that time had been a mere right to compensation the amount of which was entirely unascertained appears to me to have been converted by the order of the arbitrator into an ascertained amount of compensation, to which the appellant company became immediately entitled, plus a right to a further unascertained amount of compensation. On the principle adopted in the *Benaby* case the payment on account, to which the appellant company then became entitled, and which was paid to it, in my view, therefore, became an amount which could "be taken into account as an amount receivable due to the expropriation" and was properly included in the computation of the appellant company's income for its 1957 taxation year.

The Minister's appeal accordingly succeeds.

The appeal in respect of the re-assessment for the year 1954 will be dismissed. The appeal in respect of the 1957 re-assessment will be allowed and the re-assessment will be restored. The Minister is entitled to the costs of both appeals.

Toronto 1966 June 6-8 — Ottawa Sept. 1

BETWEEN:

WILKINSON SWORD (CANADA) LIMITED .... PLAINTIFF;

AND

ARTHUR JUDA carrying on business as CONTINENTAL WATCH IMPORT CO. .... DEFENDANT.

Trade Marks—Transfer of marks by foreign parent company to Canadian subsidiary—Sale in Canada by third party of wares purchased abroad from parent company—Wares marketed by subsidiary not fully manufactured by parent—Whether marks "distinctive"—Whether subsidiary agent of parent—Statutory right to transfer mark—Effect of—Construction of statute—Whether resulting trust of marks for parent—Whether registration of marks essential—Implied reservation in transfer for goods already sold by transferor Trade Marks Act, ss. 2(f), 2(t)(i), 19, 47.

Plaintiff's parent company, a United Kingdom company, marketed in Canada from 1920 to 1963 garden tools, razor blades, swords, etc., bearing the word mark "Wilkinson Sword" (registered in Canada in 1954) and a design mark of the same words over crossed swords (registered in Canada in 1964). In 1962 plaintiff was incorporated in Ontario as a wholly-owned subsidiary of its parent company and in 1963 commenced to distribute in Canada garden tools, razor blades and swords manufactured in England by its parent company and bearing the above trade marks In May 1963 plaintiff began to apply in Canada the final coating to the razor blades before distributing them. For a time therefore plaintiff distributed in Canada blades fully processed in England and blades partly processed in Canada, but blades of both descriptions bore the above trade marks as well as the words "Made in England", and were indistinguishable Moreover plaintiff's advertising left the implication that all the blades which it marketed were made in England by its parent company. In June 1965 the company transferred the trade marks to plaintiff and the transfer was registered. In September 1965 plaintiff brought an action for infringement of the trade marks against defendant which since February 1965 had been marketing in Canada razor blades which it had acquired in England and which had been manufactured there by plaintiff's parent company and bore the above trade marks. Defendant counterclaimed for expungement of the registrations.

Held, the trade marks were not distinctive at the time of the commencement of the proceedings bringing their validity into question since they did not "actually distinguish" plaintiff's razor blades from those of its parent as required by the definition of "distinctive" in s. 2(*f*) of the *Trade Marks Act;* and the registrations were therefore invalid under s. 18(1)(*b*). *Impex Electrical Ltd. v. Weinbaum* (1927) 44 R P.C. 405; *In re Apollinaris Company's Trade Marks* [1891] 2 Ch. 186; *Lacteosota Ltd v. Alberman* 44 R.P.C. 211; *J. Ullmann & Co. v. Leuba* (1908) 25 R.P.C. 673 (P.C.); *Wotherspoon v. Currie,* L.R. 5 E. & L. App. 508; *Anokool Chunder Nundy v. Queen-Empress* (1900) 27 I L.R. 776;

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Peggy Sage Inc. v. Siegel Kahn Co. of Canada Ltd [1935] S.C.R. 539; *Bowden Wire Ltd v. Bowden Brake Co. Ltd* (1914) 31 R.P.C. 335 (H.L.); *Robert Crean and Co. v. Dobbs and Co.* [1930] S.C.R. 307; *Wood v. Butler* (1886) 3 R.P.C. 81; *In re Hotpoint Electric Heating Co.* (1921) 38 R.P.C. 63; *Dubiner v. Cheerio Toys and Games Ltd* [1965] 1 Ex. C.R. 524; *Reddaway v. Banham* [1896] A.C. 199, discussed.

The mere fact that plaintiff was controlled by its parent company did not establish that it carried on business as agent of its parent company. *Gramophone and Typewriter Ltd v. Stanley* [1908] 2 K.B. 89, applied.

Section 47(1) of the *Trade Marks Act,* which declares that a trade mark is transferable, is not to be interpreted as intended to alter the previous law and to imply as a matter of law that any use by the transferee of a trade mark actually distinguishes his goods from those of others even though it does not do so in fact. The *Trade Marks Act* is a codification and s. 47(1) is therefore to be construed without reference to the previous law since its import is not doubtful and its language had not previously acquired a technical meaning or a special sense (*Bank of England v. Vagliano* [1891] A.C. 107, applied). If the rule in *Heydon's* case applies to permit resort to the previous law to ascertain the evil which s. 47(1) was intended to remedy, the previous law, which prohibited the transfer of a trade mark otherwise than with the goodwill of a business, was not an evil (*Eastman Photographic Materials Co. v. Comptroller-General* [1898] A.C. 571 referred to).

Held also, s. 47(2) of the *Trade Marks Act,* which relates to the question of distinctiveness where two or more persons have rights to the use of confusing trade marks as a result of a transfer, does not on the principle of *expressio unius est exclusio alterius* prevent a trade mark from being held not distinctive in other circumstances.

Semble:—

(1) The transfer of the trade marks by the parent company to its subsidiary, if made without consideration, would not give rise to a resulting trust of the marks in favour of the parent company. A trade mark by definition (s. 2(*t*)(i)) must be used to distinguish goods manufactured or sold by the owner of the mark, which in this case would be the subsidiary company as trustee, and not goods manufactured or sold by the beneficiary, which in this case would be the parent company.

(2) Registration of the transfer of a registered trade mark is not necessary to the effectiveness of the transfer under s. 47 of the *Trade Marks Act.*

(3) Section 19 of the *Trade Marks Act* confers on the "owner" of a registered trade mark the exclusive right to its use in Canada whether or not he appears on the register as owner.

(4) A reservation must be implied in a transfer of a trade mark in respect of goods already put in trade channels by the transferor.

INFRINGEMENT ACTION.

Donald J. Wright and *D. M. Plumley* for plaintiff.

Gordon F. Henderson, Q.C., Irving Goodman and *Kent Plumley* for defendant.

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JACKETT P.:—This is an action for infringement of two trade marks registered under the *Trade Marks Act,* chapter 49 of the Statutes of 1953, and a counterclaim for expungement of the registrations of the trade marks.

The plaintiff is a wholly owned subsidiary company of a United Kingdom manufacturing company. The parent company was originally named "The Wilkinson Sword Company Limited", which name was changed on May 18, 1963, to "Wilkinson Sword Limited". I shall hereinafter refer to the parent company as the "United Kingdom company".

One of the two trade marks consists of the words "Wilkinson Sword" and the other is referred to as the "Wilkinson Sword Design". I shall hereinafter refer to the two marks as "the trade marks in question".

The United Kingdom company commenced to use the word mark in 1906 and commenced to use it in Canada in 1920. From that time until 1954 it used it on, *inter alia,* wares described by it as razors, safety razors and blades therefor, dry shavers, electric shavers, swords, foils, bayonets, garden tools with a cutting edge and hunting knives. In addition to such use in the United Kingdom and Canada, it so used the word mark in the United States, Argentina, France, Spain, India, New Zealand, Chile, Italy, South Africa, Australia and Malay.[1]

The design mark was used in Canada by the United Kingdom company commencing in 1920 on "Razors, dry shavers, razor blades, scissors, a scissor-like cutter for garden and domestic use..." and "Garden tools" and in Great Britain on swords, in addition to such goods. The design consists of the words "Wilkinson Sword" superimposed upon crossed swords.[1]

The United Kingdom company at no time had any office or place of business in Canada.[1]

I infer that the use made by the United Kingdom company of the trade marks in Canada prior to 1958 consisted in sending to Canadian customers wares of its manufacture on which the trade marks were marked for the purpose of distinguishing wares made and sold by the United Kingdom company from wares manufactured and sold by others.

[1] See certified copies of registrations and section 53(3) of the *Trade Marks Act.*

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Whatever types of wares were so sold for the Canadian market in earlier years, it seems clear that in more recent years they have been restricted to garden tools, razor blades and swords.

On May 18, 1954, the United Kingdom company registered its word trade mark in Canada under the *Trade Marks Act.*

The year 1957 saw the commencement of business relations between the United Kingdom company and John A. Huston Company Limited (hereinafter referred to as "Huston") in connection with the marketing in Canada of wares of the United Kingdom company's manufacture.

Late that year, it was arranged that Huston would be the exclusive distributor in Canada of garden tools manufactured by the United Kingdom company. The first sales under that arrangement were made in Canada in 1958. For a year or so the garden tools were imported and sold in Canada by Huston as agent for the United Kingdom company. From 1962 on, however, Huston purchased the garden tools from the United Kingdom company packaged and marked with the trade marks in question and resold them in Canada in the state in which it received them from the United Kingdom company.

Early in the 1960's, the United Kingdom company started to manufacture razor blades for safety razors that had such a marked superiority over blades previously available to the public that a great demand developed for them not only in the United Kingdom but in Canada and other countries. These blades were made of stainless steel but the secret of their success was in a coating that was put on them by a finishing operation that did not change their appearance to the naked eye but converted them from an unmarketable product into a "prestige" item the demand for which was so great that for a few years it could not be completely met.

In 1961, the United Kingdom company "through" Huston, introduced these new blades to the Canadian market by a limited free distribution to retailers. That was all that was required to create a market in Canada for them.

Huston purchased the new Wilkinson Sword blades from the United Kingdom company in a fully manufactured and packaged state, with the two trade marks marked on them, ready for sale. It imported them into Canada for resale on the Canadian market from September 1961, until January 1963.

In December 1962 the United Kingdom company caused the plaintiff company to be incorporated under the *Ontario Companies Act*.

As already indicated, the plaintiff company is a wholly owned subsidiary of the United Kingdom company. The plaintiff's case depends, however, upon a recognition of the separate personalities of the two companies.[2] There was no evidence that the plaintiff acted as agent of the United Kingdom company or that the two companies so operated in association with each other, as a single trading organization or otherwise, as to create any situation from the point of view of the trade mark problems raised by this case that would not exist if there was no shareholding relationship between them (I rejected an argument to the contrary by the defendant without calling on counsel for the plaintiff). The plaintiff's rights must therefore be determined, as its counsel agreed during the course of the trial, on the basis that the two companies had no continuing relationship except that of vendor and purchaser. It is important that that be borne in mind in appraising the facts in this case, having regard to the similarity of the corporate names of the United Kingdom company and the plaintiff.

In January 1963 Huston ceased purchasing razor blades from the United Kingdom company. Commencing in that month, the plaintiff purchased, from the United Kingdom company, blades completely manufactured, marked with the two trade marks, packaged and ready for sale, imported

[2] As will subsequently appear, the infringement alleged against the defendant consists in selling in Canada goods that had been manufactured by the United Kingdom company and on which the United Kingdom company had put the trade marks in question Obviously that would have been no infringement if the plaintiff and its parent are to be regarded as part of a single entity for trade mark purposes for it cannot be an infringement to resell, in association with a trade mark, goods that have been acquired in the ordinary course after they have been put in trade channels by the owner of the trade mark.

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them, and resold them to Huston who continued to distribute them in Canada as it had been doing when it imported them itself.

The plaintiff also, since its incorporation, has imported garden tools and swords made by the United Kingdom company, imported them into Canada with the trade marks in question already marked thereon and resold them in Canada in the state in which they were so received and imported.

In March of 1963, agreements were executed by Huston and the plaintiff whereby Huston undertook the management of the plaintiff and obtained exclusive selling rights for "shaving products and garden tools" produced or distributed by the plaintiff. Under the management agreement, Huston supplied "technical and production management personnel" and supervised and managed the business operations of the plaintiff.

The situation from that time forward was therefore that the United Kingdom company was selling wares to the plaintiff which it controlled and with which, therefore, it did not deal at arm's length, and the plaintiff was selling wares to Huston although the management of the plaintiff was supplied in fact by the persons who constituted the management of Huston. There was, therefore, a very special situation from the point of view of inter-company relations but none of this is, as I appreciate the matter, relevant from the point of view of the problems raised by this case.

In May 1963 the plaintiff commenced buying from the United Kingdom company, the razor blades in the state in which they were before the final finishing operation had put on them the coating that was the secret of their commercial success, importing the blades in such state and carrying on in Canada the operations whereby such finishing coat was put on the blades and whereby the blades were packaged and prepared for the retail market.[3] In the case

[3] Considerable evidence was given as to the control exercised by the United Kingdom company to ensure that such blades would be the same as though manufactured entirely by that company. I can see that such evidence would be relevant if the trade marks in question were "certification marks" (section 2(*a*)) or if the plaintiff had been a "registered user" (section 49). As it is, I cannot see how that evidence is material.

of blades so prepared for market, the trade marks in question had been put on the blades by the United Kingdom company before they were sold by that company to the plaintiff but were put on the packaging by the plaintiff. I shall hereinafter refer to blades so prepared for market as blades made in the United Kingdom and processed and packaged in Canada to distinguish them from blades that were made, processed and packaged in the United Kingdom. (In so doing I am not to be taken to be expressing any view as to whether the blades that I refer to as processed and packaged in Canada were "manufactured" by the plaintiff.)

The blades made in the United Kingdom and processed and packaged in Canada, as far as the naked eye, even of an expert, is concerned, appeared exactly the same as those that were made, processed and packaged in the United Kingdom. Furthermore, in each case, the blade itself bore the words "Made in England" whether the final processing and packaging was done in England by the United Kingdom company or in Canada by the plaintiff.

Until July 18, 1963 the plaintiff sold to Huston blades made, processed and packaged in the United Kingdom. From that date forward, the plaintiff sold to Huston blades made in the United Kingdom and processed and packaged in Canada. On or before that day, the plaintiff ceased importing blades made, processed and packaged in the United Kingdom. From July 18, 1963 until such time as its stocks of blades acquired before that time were exhausted, Huston was distributing in Canada blades made, processed and packaged in the United Kingdom and blades made in the United Kingdom and processed and packaged in Canada. Similarly, since that day, retailers in Canada have been selling both blades made, processed and packaged in the United Kingdom and blades made in the United Kingdom and processed and packaged in Canada and will continue to do so until such time as the blades made, processed and packaged in the United Kingdom disappear from their stocks. In both cases, blades of each kind are marked with the trade marks in question and in neither case were any of the blades so marked or packaged that a member of the

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Canadian purchasing public could distinguish the blades of one kind from those of another or the packages in which one kind were prepared for sale from those in which the other kind were prepared for sale.

Prior to July 1963 neither the plaintiff nor Huston did any advertising of the blades in Canada except that involved in the distribution of the blades with the United Kingdom company's two trade marks marked on them and their packaging.

In that month, the plaintiff and Huston started advertising on a large scale and such advertising continued until the time of the trial. No such advertising was designed to inform the public that the manufacturer of the blades being advertised for sale in Canada in association with the trade marks in question after July 1963 was different from the manufacturer of the blades sold in Canada in association with such marks before that time and from the manufacturer of the swords and garden tools so sold both before and after that time. Indeed, while the advertising that has been brought to the attention of the Court contains no explicit statement as to the identity of the manufacturer of the goods being advertised (or, indeed, any specific reference to the United Kingdom company, the plaintiff or Huston) there is, as I read such advertising an obvious implication

(a) that the blades being advertised for sale in Canada after July 1963 were made in England, and

(b) that such blades were made by the manufacturer of Wilkinson Sword (see, for example, the newspaper advertisement depicting very prominently a ceremonial sword with the trade marks in question stamped into the sword blade and immediately under it a picture of a Wilkinson Sword razor blade and a statement to the effect, *inter alia,* that this—"The World's finest razor blade"—"could only have come from the craftsmen of Wilkinson Sword") which, in fact, have always been made in England by the United Kingdom company.

Furthermore, the television advertising of the blades by the plaintiff and Huston was so got up, generally speaking, as to convey the idea that there was a connection between the fact that the manufacturer was a sword-making company and its ability to produce fine blades.

On June 19, 1964 the United Kingdom company registered its design mark in Canada under the *Trade Marks Act*.

From February 19, 1965 to August 9, 1965 the defendant purchased in England razor blades made, processed and packaged in England by the United Kingdom company (and therefore bearing the trade marks in question) and imported them and sold them in Canada. Between August 9, 1965 and the commencement of this action, the defendant imported and sold such blades but there is nothing in the record to indicate whether the blades sold by the defendant in Canada during this period were acquired by the defendant while the United Kingdom company was owner of the trade marks. Since the commencement of this action, the defendant has acquired such blades in England, imported them and sold them in Canada and the defendant proposes to continue so purchasing, importing and selling such blades unless restrained by order of the Court.

On June 21, 1965 the United Kingdom company executed a transfer of the two trade marks to the plaintiff. On July 2, 1965 the defendant received a letter from the plaintiff's solicitors bearing date June 29, 1965 informing him of the assignment of the trade marks, stating that the sale in Canada of razor blades bearing the trade marks and not purchased from the plaintiff is an infringement of the plaintiff's rights and warning that the plaintiff intended to take prompt legal action to restrain any infringement. The transfer was registered under the *Trade Marks Act* on August 9, 1965.

The facts that I have outlined up to this point reveal the question that arises between the parties, as I understand it, namely: Can the plaintiff, by virtue of the transfer to it of its parent's Canadian trade marks, prohibit third persons from importing and selling in Canada goods manufactured abroad by the parent and bearing the trade marks placed thereon by the parent?[4]

[4] For a similar attempt to use trade marks to monopolize a market for goods of a particular class, see *In re Apollinaris Company's Trade-Marks*, [1891] 2 *Ch.* 186 at pages 225 *et seq.*, and pages 229 *et seq.*

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This action was instituted on September 7, 1965. On October 18, 1965 the defendant filed a statement of defence and counterclaim whereby it, *inter alia,* brought into question the validity of the registrations of the plaintiff's trade marks. Pursuant to a consent order, the defendant, on March 31, 1966 filed an "amended" statement of defence and counterclaim.

The plaintiff's case, as pleaded, is simply

(a) that it is, and has been since *August 9, 1965,* the registered owner of the two registered trade marks,

(b) that it "has, since July 1963 produced and sold razor blades throughout Canada in large numbers in association with the said trade marks", and

(c) that the defendant has imported into and distributed in Canada razor blades to which the two trade marks have been applied "but which are not wares of the plaintiff" and has thereby infringed the exclusive right of the plaintiff to the use of the trade marks.[5]

During the course of the hearing, counsel for the plaintiff put his case on the plaintiff being owner (not *registered owner*) of the *registered trade marks,* maintained that the plaintiff's exclusive rights to the marks arose on the execution of the transfer on June 21, 1965 and claimed judgment in respect of infringements on and after July 2 when the defendant was informed of the transfer. He did not, however, seek any amendment to the statement of claim although it clearly makes a claim for infringement of the plaintiff's rights as registered owner since August 9, 1965.[6]

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[5] The trial proceeded upon the basis that, upon the plaintiff establishing at least one act of infringement and satisfying the Court that it had sustained some damage, the question of what further infringements, if any, had been committed and of damages or profits would be the subject matter of a reference.

[6] Had he done so, subject to what counsel for the defendant might have said, I should have given the request favourable consideration because, as far as I can see, there is no possibility of the defendant having suffered prejudice by such a change of pleading during the course of the trial (unless, indeed, as well may be, the defendant agreed to certain facts limited to a period of time prior to August 9, 1965, to which it would not otherwise have been prepared to agree without making much more careful investigation as to what actually happened).

The defendant denies any infringement of the two trade marks and calls in question their validity. The substantive part of the statement of defence, which it is impossible to summarize, reads as follows:

2. The Defendant denies that he has imported into and distributed in Canada razor blades bearing trade marks to which the Plaintiff has or had the exclusive rights and denies that he has infringed any rights of the Plaintiff whatsoever, for the reasons hereinafter set forth.

3. The Defendant admits that the Plaintiff is registered as owner by Assignment of Canadian Trade Mark Registrations Nos. N S. 197/50113 and 136,228, and admits that the assignment document dated June 21, 1965 and recorded in the Trade Marks Office on August 9, 1965, was duly executed by the authorized signing officers of Wilkinson Sword Limited. The Defendant, however, denies the validity of such registrations, including the validity of the trade marks themselves and also the validity of the assignment thereof to the plaintiff, for the reasons hereinafter set forth.

4. (a) The Defendant states and the fact is that all of the razor blades purchased by him and imported into and sold in Canada are legitimate and genuine products of the Plaintiff's parent company, Wilkinson Sword Limited. The Defendant alleges that, having purchased these razor blades, which are the genuine product of the parent company of the Plaintiff, he is entitled to import same into and sell same in Canada.

(b) The Defendant states and the fact is that the Plaintiff is a wholly-owned and wholly-controlled subsidiary of its parent company in England, Wilkinson Sword Limited; that both are part and parcel of one trading organization; that the Plaintiff does not and never has acted independently of its parent company; and that the Plaintiff has acted solely as the Agent of and on behalf of its parent company in regard to all matters in issue herein. Accordingly, all rights alleged to be vested in the Plaintiff by reason of trade mark registrations and assignment, if such are valid at all, which is not admitted but denied, can only be vested in the Plaintiff's parent company, Wilkinson Sword Limited. Accordingly, the Plaintiff has no right to take any action against the Defendant for the sale of razor blades all of which are the genuine product of its parent company.

(c) The Defendant states that if the trade marks and/or assignment thereof are valid, which is not admitted but denied, that such assignment to the Plaintiff gives the Plaintiff no further rights than its parent company, Wilkinson Sword Limited had as a result of such trade mark registrations. Inasmuch as its parent company, Wilkinson Sword Limited, has no right to sue the Defendant in regard to goods sold by the Defendant in Canada which are legitimate and genuine products manufactured by Wilkinson Sword Limited, then neither does the Plaintiff have any such rights. The Defendant alleges that the Trade Mark Act does not allow and was not designed to allow persons to set up such exclusive arrangements between parent and subsidiary companies by which a subsidiary company can prevent any other person from importing and/or selling in Canada the legitimate and genuine goods of its parent company. Accordingly, no such rights can or do flow from the assignment of the trade marks to the Plaintiff.

5. (a) The Defendant alleges that the assignment of the two trade marks in issue herein is invalid because such assignment was executed by Wilkinson Sword Limited, the British parent company of the Plaintiff, in favour of the Plaintiff, for no consideration and because Wilkinson Sword Limited retains complete control over the trade marks and can at any time obtain a re-assignment from the Plaintiff herein. Accordingly, it is evident that the Plaintiff holds the trade mark rights in Canada in issue herein only as an Agent and/or Trustee for its parent company, Wilkinson Sword Limited and, therefore, such assignment is invalid and totally void.

(b) The Defendant alleges that the assignment of the trade marks in issue herein is invalid because the purpose of such assignment was not for a purpose contemplated by the Trade Marks Act but solely for the purpose of attempting to restrain the importation into and sale in Canada of blades purchased from the Plaintiff's parent company or other associated companies. As this assignment was made solely for this improper purpose, it is, therefore, totally invalid and void.

6. (a) The Defendant alleges, and the fact is, that the words "Wilkinson Sword", and the design of crossed swords, do not distinguish the products of either the Plaintiff or its associated companies from those of others, for the following reasons. The Defendant alleges and the fact is that if such words and/or design ever did distinguish anything at all, which is not admitted but denied, then they distinguish and at all times have distinguished only razor blades manufactured by Wilkinson Sword Limited, the British parent company of the Plaintiff, irrespective of by whom such razor blades have been finished, packaged and/or sold, and have at no material times distinguished razor blades as having been finished, packaged, and/or sold by the Plaintiff, and such trade marks are not and at no material time were distinctive of razor blades finished, packaged and/or sold by the Plaintiff.

(b) The Defendant alleges and the fact is that, in any event, since about July 1963 the words "Wilkinson Sword" and the design of crossed swords, as applied to razor blades, do not distinguish any products whatsoever, for the following reasons. The Defendant states and the fact is that until July 1963 all razor blades bearing the said trade marks that were sold in Canada were completely manufactured and packaged by Wilkinson Sword Limited, the British parent company of the Plaintiff Such razor blades were originally sold in Canada by Wilkinson Sword Limited through its exclusive distributor, the John A. Huston Company Limited, until January 1963. From January 1963 until late in the spring of 1963, such razor blades, which were still completely manufactured and packaged by Wilkinson Sword Limited, were imported into Canada by the Plaintiff herein and then resold to the John A. Huston Company Limited, who continued to act as sole distributor in Canada for such razor blades.

In or about July 1963 the Plaintiff began to put on the Canadian market razor blades which it had imported from England, having purchased same from its British parent company, Wilkinson Sword Limited in a raw or unfinished state, and which razor blades had been finished, processed and packaged by the Plaintiff in Canada. Such razor blades already bore the trade marks of Wilkinson Sword Limited, having been applied to the razor blades during the first part of the manufacturing process which was done by Wilkinson Sword Limited in England. These blades which bore the trade marks of Wilkinson Sword Limited, the British parent company of the Plaintiff, were partially manufactured in England by such parent company and partially manufactured and packaged in Canada by the Plaintiff herein, and were sold in Canada by the Plaintiff herein bearing the trade marks of the British parent company, Wilkinson Sword Limited, despite the fact that these products were not products of Wilkinson Sword Limited.

Wilkinson Sword Limited, the British parent company of the Plaintiff herein acquiesced in and allowed these razor blades, which were not its product, to be put on the Canadian market, although any rights to the trade marks in question herein remained the property of Wilkinson Sword Limited until at lease [*sic*] June 21st 1965

During the summer of 1963, both types of blades were present on the Canadian market, the original genuine product manufactured by Wilkinson Sword Limited, and the product imported in an unfinished state and finished, processed and packaged by the Plaintiff herein, and both of these types of blades bore the trade marks referred to herein. Again, during the early part of 1965, the Defendant states and the fact is, that he imported into and sold in Canada razor blades bearing the trade marks in issue herein, which were the genuine product of Wilkinson Sword Limited, who were, at this time, still the owners of any trade mark rights therein Accordingly, at this time there were again two types of blades on the Canadian market, the genuine products of the trade marks owner, Wilkinson Sword Limited, and the blades of the Plaintiff.

As a result of these facts the Defendant alleges, and the fact is, that the trade marks in issue herein ceased to be distinctive as early as July 1963, and lost their validity

(c) The Defendant alleges, and the fact is, that the Plaintiff has been, since July 1963 deceiving and misleading the Canadian public into thinking that the razor blades that the Plaintiff sells are the genuine products of its British parent company, Wilkinson Sword Limited The Defendant alleges and the fact is, that the Plaintiff has never in any way advised the Canadian public of the change that took place in the manufacture of the razor blades sold by it in Canada, which change took place at about the beginning of the summer of 1963; that the Plaintiff has deliberately misled the Canadian public in this regard and that it continues to do so, intending to trade on the reputation of its British parent company, Wilkinson Sword Limited, and on the reputation of the stainless steel razor blade which was manufactured originally only by Wilkinson Sword Limited, and that the Plaintiff has intended to and has in fact misled the Canadian public into thinking that the razor blades being sold by the Plaintiff in Canada are still the legitimate and genuine product of its British parent company, Wilkinson Sword Limited.

The Defendant alleges, and the fact is, that Wilkinson Sword Limited has acquiesced in and allowed this distribution to go on during the past two years and more.

Accordingly, the Defendant alleges that the trade marks in question herein have lost their validity.

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Upon the opening of his argument, counsel for the defendant summarized his attack on the validity of the two registered trade marks[7] as being

(a) an attack, under section 18(1)(*b*) of the *Trade Marks Act,* based upon a contention that they were not, at the time of the commencement of these proceedings, "distinctive" within the meaning of that word as defined by section 2(*f*), and

(b) an attack based upon the fact that the trade marks were being used to deceive the public.

He, at the same time, summarized his defence of no infringement under three heads, *viz,*

(a) the defendant's importation and sale of goods manufactured by the United Kingdom company with the trade marks attached had the implied licence of the United Kingdom company and the trade marks distinguished the goods of associated companies of whom the United Kingdom company was one,[8]

(b) the transfer of the trade marks in question was without consideration and there was therefore a resulting trust in favour of the United Kingdom company so that a sale in Canada of goods manufactured and sold by that company under the trade marks was not an infringement of them,

(c) sales by the defendant before August 9, 1965 the day on which the plaintiff became registered as owner of the trade marks, do not constitute infringements

(i) because the statement of claim is for infringement of a title expressed to commence on that day, and

[7] Some reference was made during argument to the decision of this Court in *Remington Rand Limited v. Transworld Metal Company Limited,* [1960] Ex. C.R. 463, where the facts were similar to the facts in this case. However, as my brother Thurlow pointed out at page 464, the validity of the plaintiff's registered trade mark was not attacked in that case.

[8] A contention that is raised by the first sentence of paragraph 4(*c*) of the statement of defence was not raised in the defendant's counsel's outline of his position at the opening of his argument. Assuming that there is a transfer of a trade mark by a manufacturer who has, before the transfer, put wares of his manufacture in trade channels with the trade mark on it, I should have thought that the transfer would not operate to prevent persons who had acquired such goods in the ordinary course of trade from selling them.

(ii) because, in any event, the plaintiff's rights by virtue of the transfer did not arise until August 9, 1965 when the transfer was registered under the *Trade Marks Act*;

and the plaintiff had failed to establish that sales between August 9, 1965 and the commencement of the action on September 7, 1965 were not of wares acquired by the plaintiff before the United Kingdom company ceased to be owner of the trade marks in question, in which event there would be a right to sell such goods notwithstanding the transfer of the marks to the plaintiff.[9]

As I have come to the conclusion that the trade marks were not "distinctive" at the time of the commencement of the proceedings bringing the validity of the marks into question and that the registrations of the trade marks are, therefore invalid, it is not necessary for me to come to any final conclusion with regard to any of the other questions raised. I propose, therefore, to indicate at this stage, very briefly, how, as I view them without more mature consideration, I would decide them.

As already indicated, I decided, during the course of the trial, that there was no evidence upon which it could be held that the plaintiff and the United Kingdom company were carrying on business jointly or that one of them was acting as agent for the other. I did not regard the authorities cited for the defendant in this connection as establishing any principle other than that laid down by the Court of Appeal in England in *Gramophone and Typewriter Limited v. Stanley*, [1908] 2 K.B. 89, which was one of the authorities upon which the defendant relied.[10]

I also, as I see it now, would have difficulties in applying the concept of resulting trust to the facts of this case. If

[9] Assuming that the defendant were successful on this point alone, a question would arise as to whether the plaintiff is entitled, in these proceedings, as presently framed, to an injunction as though it were a *quia timet* action. I need not decide this question.

[10] The view upon which I acted at that time, and which still seems to me to be sound law is that the mere fact that one incorporated company controls another is not sufficient by itself to establish that the controlled company carries on business as agent of the controlling company.

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I had to decide this point, I should have to study very carefully the views expressed by my brother Noël in *Dubiner v. Cheerio Toys and Games Ltd.*, [1965] 1 Ex. C.R. 524 at pages 554 *et seq.* My present difficulty is that I do not see how it is possible for the owner of a trade mark as defined by subparagraph (i) of section 2(*t*) of the *Trade Marks Act* to hold such a trade mark in trust for some other person (except in the case where the trustee owns all the assets of a business, including the trade marks associated therewith, in trust for beneficiaries and operates that business in his capacity as trustee for the benefit of the beneficiaries).[11] Under our law of trusts, the trustee is the owner but is bound by equity to hold the trust property and all the fruits of it for the beneficiaries. By statutory definition, the kind of trade mark that we are discussing is a mark that is used "so as to distinguish" goods manufactured or sold by the *owner* of the mark. It cannot be used to distinguish goods manufactured or sold by somebody else. Compare section 2(*f*) of the *Trade Marks Act.* If, therefore, I had to apply the trust concept here it would seem to me that I should have to conclude that a trade mark owned by the owner as trustee would have to be used to distinguish goods manufactured or sold by him as trustee, and not goods manufactured or sold by the beneficiary of the trust.

With reference to the plaintiff's right to rely on sales in Canada prior to August 9, 1965 as acts of infringement, if the only question were the state of the statement of claim, I should be prepared to hear an application for leave to amend even at this late date. Furthermore, I am inclined, as I see it now, to accept the submission of counsel for the plaintiff

(a) that registration of the transfer is not necessary to make a transfer of a registered trade mark effective under section 47,[12] and

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[11] One of my doubts is whether it is possible to carry on a business as trustee in the absence of special statutory or contractual status.

[12] Compare *Ihlee v. Henshaw,* (1886) 31 Ch D. 323 per North J. at page 324. See also *The Magnolia Metal Company v. The Atlas Metal Company and Others,* (1897) 14 R.P.C. 389 and *Blightly Industries Association Ld. v. The Scottish Home Industries Association, Ld.,* (1927) 44 R.P.C. 269.

(b) that section 19 confers on the "owner" of a registered trade mark the exclusive right to its use in Canada whether or not he appears on the register as owner.

With reference to the goods sold in Canada after August 9, 1965 and before the commencement of the action, I am inclined to the view that there must be implied a reservation in a transfer of a trade mark in respect of goods already put in trade channels by the transferor (see footnote #8) and that the onus was on the plaintiff to plead and establish that the infringements complained of were not sales of such goods.

The remaining submission of counsel for the defendant, before I come to section 18(1)(*b*), is that there have been such misrepresentations by the plaintiff in the use of the trade marks transferred to it as to invalidate the trade marks. As I see it at the moment, such misrepresentations (e.g. that the goods finished and packaged by the plaintiff are wares manufactured by the United Kingdom company) is not a separate head of invalidity under our Act. It may well, however, be a relevant circumstance in deciding the question raised under section 18(1)(*b*).

I turn now to section 18(1)(*b*) which reads, in part, as follows:

> 18. (1) The registration of a trade mark is invalid if
>
> . . .
>
> (*b*) the trade mark is not distinctive at the time proceedings bringing the validity of the registration into question are commenced;
>
> . . .

The question under section 18(1)(*b*) is whether the trade marks were distinctive "at the time proceedings bringing the validity of the registration(s) into question" were commenced. Whether that time in this case is the date that the action was instituted, September 7, 1965, the date that the original statement of defence and counterclaim were filed, October 18, 1965, or the date that the amended statement of defence and counterclaim were filed, March 31, 1966, is not, as I apprehend the facts, a matter upon which I must reach any conclusion in this case. I shall deal with

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the matter as though the relevant time were the period from September 7, 1965 to March 31, 1966, because I can detect no change in the material state of affairs during that period.

I propose, therefore, to consider whether, during the period from September 7, 1965 to March 31, 1966, the trade marks in question were "distinctive" within the meaning of that word as defined by section 2(*f*) of the *Trade Marks Act*, which reads:

> 2. In this Act,
>
> . . .
>
> (*f*) "distinctive" in relation to a trade mark means a trade mark that actually distinguishes the wares or services in association with which it is used by its owner from the wares or services of others or is adapted so to distinguish them;

The question that I must answer is whether the trade marks in question, during the period from September 7, 1965 to March 31, 1966, *actually distinguished* the razor blades processed and packaged by the plaintiff from the wares of "others". In doing so, I must bear in mind that the United Kingdom Company falls within the class of "others" because, as I have already indicated, that is the foundation of the plaintiff's case against the defendant and is the only conclusion that, in my view, can be reached on the material before the Court.

In my view, it is beyond dispute that, on the facts that have been placed before the Court, the trade marks in question did not during the relevant period "actually distinguish" the plaintiff's razor blades from the wares of others and I must therefore hold that the trade marks were not "distinctive" at any time during that period. Accordingly, I hold that their registrations were invalid by virtue of section 18(1)(*b*).

A brief reference to the facts will suffice to show why I feel constrained to reach that conclusion.

For a period of over forty years, from 1920 until July 1963, these two very striking trade marks were used in Canada to distinguish wares—garden tools, swords and razor blades—manufactured by a particular manufacturer

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in England.[13] Following such a prolonged exposure of the Canadian purchasing public to these marks as indicating the goods of a particular manufacturer in England,[14] in July 1963 the plaintiff started to introduce into trade channels in Canada, under the same marks, razor blades that were only partly manufactured by the manufacturer whose wares such marks had previously identified and that were partly manufactured by the plaintiff, without in any way indicating to the members of the Canadian purchasing public that such goods were not the razor blades—manufactured by a manufacturer in England in whose wares they had pre-

[13] Compare *Impex Electrical Ld. v. Weinbaum,* (1927) 44 R.P.C. 405 per Tomlin, J. at page 410: "If a manufacturer having a mark abroad has made goods and imported them into this country with the foreign mark on them, the foreign mark may acquire in this country this characteristic, that it is distinctive of the goods of the manufacturer abroad. If that be shown, it is not afterwards open to somebody else to register in this country that mark, either as an importer of the goods of the manufacturer or for any other purpose. The reason of that is not that the mark is a foreign mark registered in a foreign country, but that it is something which has been used in the market of this country in such a way as to be identified with a manufacturer who manufactures in a foreign country. That, I venture to think, is the basis of the decision in the *Apollinaris* case ([1891] 2 Ch. 186). It seems to me to be the basis of the decision in the case before Mr. Justice Clauson of *Lacteosote Limited v. Alberman* (44 R.P.C. 211) and it seems to me to be consonant with good sense." Contrast *J. Ullmann & Co. v. Leuba,* (1908) 25 R.P.C. 673 (P.C.) where the Hong Kong trade mark denoted in Hong Kong the goods of the Hong Kong retailer and not the goods of the foreign manufacturer who supplied them to him.

[14] Whether or not the individual members of the purchasing public were aware of the United Kingdom company's name is immaterial—the theory is that those who had shown a preference for the goods sold under the marks had learned to have confidence in the manufacturer of such wares regardless of whom he might be. See *Wotherspoon v. Currie, L.R.* 5 E. & I. App. 508, per Lord Hatherley, L.C. at pages 514-15: "Therefore the name 'Currie' ought to be distinct, as I believe it is, and the name of the article again, if it has acquired a name, should not, by any honest manufacturer, be put upon his goods if a previous manufacturer has, by applying it to his goods, acquired the sole use of the name. I mean the use in this sense, that his goods have acquired by that description a name in the market, so that whenever that designation is used he is understood to be the maker, *where people know who the maker is at all*—or if people have been pleased with an article, it should be recognized at once by the designation of the article, although the customers may not know the name of the manufacturer. It may very well be that hundreds of people like Glenfield Starch, and order it because they think that it is the best starch that they ever used, without having heard the name of Mr. Wotherspoon, and without knowing him at all. They say, I want the thing that bears that name, the thing made in a particular way, made by the manufacturer who makes it in that way, and there being only one manufacturer who does make it in that way, I want the article made by that manufacturer."

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sumably learned to have confidence—that they had been previously purchasing under the same trade marks. (I should have been inclined to have reached the conclusion that the blades so finished by the plaintiff were nevertheless still manufactures of the United Kingdom company, and that there was therefore no change in substance in what was being distributed in Canada under the trade marks, were it not for the fact that both parties take the position—by their pleading and by submission of counsel—that the blades sold by the plaintiff after July 1963 were blades manufactured by it and not by the United Kingdom company.) Commencing, therefore, in July 1963, as a result of the acts of the plaintiff, there were in trade channels in Canada, razor blades reaching the Canadian purchasing public under the trade marks in question some of which were manufactured by the United Kingdom company in England and some of which were (as I must find for the purpose of this case) manufactured by the plaintiff in Canada and there was no means whereby the purchasing public could know that all such blades were not manufactured by the manufacturer in England in whose wares their previous experience with the trade marks in question would lead them to have confidence.[15] Indeed, each blade—those made by the plaintiff in Canada as well as those made by the United Kingdom company—bore the words "Made in England" and there was no advertising at any

[15] Compare *Anookool Chunder Nundy v. Queen-Empress,* (1900) 27 I.L.R., Calcutta 776 per MacPherson and Hill, JJ. at page 780: "Assuming however that this mark, being the trademark of the Chartered Mercantile Bank of India, London and China, could after that Bank ceased to do business become by user the trade-mark of the Mercantile Bank of India, there is in this case no sufficient proof of the user necessary to effect that. A mark to be a trade-mark must be a mark used for denoting that the goods are the manufacture or the merchandize of a particular person and the particular person in this case is according to the charges the Mercantile Bank of India. The prosecution had, therefore, to prove that this mark was used for denoting that the gold bars were the manufacture or merchandize of that Bank. The mark in itself does not denote anything of the kind, and it is not necessary that it should do so. But it was originally used to denote something else, and there is no evidence that it had acquired in the market any other meaning or that it was understood to denote that the gold bars upon which it was impressed were the gold bars imported by the Mercantile Bank of India"

As to the possibility of circumstances requiring the publishing of information as to ownership of a trade-mark to avoid confusing the public, see *Peggy Sage Inc. v. Siegel Kahn Company of Canada Limited,* [1935] S.C.R. 539 at page 549.

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relevant time to the Canadian public, either connected with the goods as distributed or otherwise, that would give the public any indication that an increasing proportion of the blades that they were getting under the trade marks in question, which were still registered in the name of the United Kingdom company, were actually manufactured in Canada by a Canadian manufacturer. In addition, at this same time—after July 1963—garden tools and swords manufactured in England by the United Kingdom company were being put into trade channels in Canada by the plaintiff under the same two trade marks.[16]

In the period during which this situation prevailed, I can only infer that the trade marks in question signified to the Canadian purchasing public that the goods associated with the marks in question were manufactured by whatever manufacturer in England had been making the goods that they had been buying in association with such trade marks for over forty years.[17]

During the period from July 1963 to June 1965, when the plaintiff was putting into trade channels some goods—garden tools and swords—manufactured by the United Kingdom company and some goods—razor blades—manufactured by the plaintiff, all under the two trade marks belonging to the United Kingdom company, the defendant imported and sold in Canada, under the same two trade marks, razor blades manufactured and sold by the United Kingdom company. Such importation and sale in Canada was quite legal and proper as far as the trade marks in question are concerned.

The situation in which the plaintiff was putting into trade channels in Canada under trade marks belonging to the United Kingdom company some goods manufactured by the

16 During this period after July 1963, while the trade marks in question were still owned by the United Kingdom company, I can find no material difference between the facts of this case and those in *Bowden Wire Ld. v. Bowden Brake Company Ld.*, (1914) 31 R.P.C. 385 (H.L.) where it was held that the owner of a trade mark had made it invalid by permitting a related company to use it on the latter company's goods.

17 Compare *Robert Crean and Co. Ltd. v. Dobbs and Co.*, [1930] S.C.R. 307. See also *Wood v. Butler*, (1886) 3 R.P.C. 81 per Fry, L.J. at page 92. " . . . where a person uses a word and represents that word to be applicable to the product of a manufacturer . . . other than himself, so as to produce the belief that the goods are the manufacture of that third person . . . , he cannot say that the word is distinctive of his own manufacture".

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United Kingdom company and some goods manufactured by itself continued until June 22, 1965, when the United Kingdom company transferred the two trade marks to the plaintiff. From that time until the commencement of these proceedings, and indeed until the trial, the plaintiff continued to put into trade channels in Canada, in association with the trade marks in question, some goods manufactured by the United Kingdom company (garden tools and swords) and some goods manufactured by the plaintiff (razor blades) without in any way[18] indicating to the Canadian purchasing public that the trade marks were now being used to mean anything other than that which they had meant in the past—namely, that *all* the wares with which they were associated were wares of the manufacturer whose wares had been marketed in association with such marks prior to 1963. (It might presumably have been intended by the plaintiff that the trade marks indicate only that the goods were goods *sold* by the plaintiff—the only representation that could truthfully have been made with reference to the garden tools and the swords as well as the blades. This might have been sufficient to make their use by the plaintiff use as trade marks as defined by section 2(*t*)(i); I make no finding on that. The question here, however, is whether they "actually" distinguished the plaintiff's goods within section 2(*f*) and there is not a scintilla of evidence of any effort to educate the Canadian purchasing public to understand that the trade marks in question, after June 1965, were used only in association with goods sold by the plaintiff.)[19]

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[18] I do not regard certain references to the Canadian company that were placed in positions on the packages where they were almost certain not to be noticed as being of any relevance for the purpose of this review.

[19] The plaintiff placed considerable reliance upon section 48 of the *Trade Marks Act* which provides, in effect, in part, that if a mark is used as a trade mark for the purpose of distinguishing wares *sold* by him, it shall not be held invalid "merely on the ground" that he or a predecessor in title has used it for the purpose of distinguishing wares *manufactured* by him. This section does not, as I read it, change the approach that has to be made in particular circumstances under section 18(1)(*b*) apart from it. In this connection, I regard as applicable to the current Canadian Act what was said by P. O. Lawrence, J. in *In re Application by The Hotpoint Electric Heating Company,* (1921) 38 R.P.C. 63 at page 71: "It is argued . . . that . . . the mark ought not to be registered, because it is deceiving the public into the belief that the goods which had become known as those of the manufacture of the Hotpoint Company were really being manufactured by a different manufacturer; and, if it did not deceive them, it at all events

There is no indication of any material change in the way in which goods were put by the plaintiff in Canadian trade channels in association with the trade marks in question during the period before the filing of the amended statement of defence and counterclaim or of any change in the appreciation of the purchasing public, during that period, as to the significance of such marks.

In these circumstances, the only inference I can draw is that the trade marks during all relevant periods "actually" —but falsely—indicated, after June 21, 1965 to the Canadian purchasing public, as they indicated during the period of over forty years before that time, that the goods with which they were associated were goods *manufactured* by some United Kingdom company—whether or not they knew its name. There is not one bit of evidence to indicate that the trade marks "actually", at any relevant time, indicated, to the Canadian purchasing public, that the wares to which they were attached were wares of the plaintiff—either as manufacturer or seller—or even that such wares were wares manufactured or sold by some unidentified person *other than* the manufacturer of the wares in association with which the marks had been used in Canada from 1920 to 1963. The trade marks in question, at no time, distinguished wares of the plaintiff as manufacturer or vendor from wares of the United Kingdom company or any other person.

In my view, there can be no question as to the correct answer to the question raised by section 18(1)(*b*) read

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would lead to confusion in the minds of the public as to who were the real manufacturers of these goods. I can conceive circumstances where the manufacturer has gained a reputation with reference to certain goods under a particular mark and ceases to manufacture those goods but hands over the manufacture to other persons and still sells the goods under the mark which he used when he himself manufactured the goods. Under those circumstances he might possibly lose the right to the mark, and it might become descriptive. It is quite true that a mark can indicate the seller or selector of the goods and need not necessarily indicate the manufacturer, but if the reputation of the mark has been gained owing to its being used by the manufacturer, and it has become known as the manufacturer's mark, I think it might very well cause deception and confusion, if it were used afterwards, without something on the mark itself, for the purpose of indicating only the seller of the goods which were being manufactured by somebody else". All that section 48 says is that a trade mark shall not be held invalid *"merely"* on the ground that it was previously used for a purpose other than its current use: It does not say that it will be valid even if it does not actually distinguish the wares of its owner as required by section 18(1)(*b*) as a condition to the validity of its registration.

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with section 2(*f*) if that question is to be answered as a question of fact.[20] Indeed, counsel for the plaintiff did not really contest the result as a finding of fact on the evidence.

What counsel for the plaintiff says, and this is really the nub of his case, is that there is an implication from subsection (1) of section 47, which authorizes transfers of trade marks, that, when a transferee uses a trade mark after it is transferred to him, there is *a presumption of law* that the trade mark "actually distinguishes" his wares regardless of what significance it may have *in fact* for members of the Canadian purchasing public.[21] His contention, as I understand it, is that such an implication must flow from section 47 for, otherwise, the section has failed to achieve any substantive change in the law.[22]

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20 See *Dubiner v. Cheerio Toys and Games Ltd.,* [1965] 1 Ex. C.R. 524 per Noel J at page 549

21 This, as it appears to me, would be to imply an intention by Parliament to nullify the "fundamental rule" that "one man has no right to put off his goods for sale as the goods of a rival trader, and he cannot, therefore ... be allowed to use ... marks ... by which he may induce purchasers to believe that the goods which he is selling are the manufacture of another person". See *Reddaway v. Banham,* [1896] A C. 199 at page 209 where Lord Herschell adopts a passage from Lord Kingsdown in the *Leather Cloth* case. That Parliament impliedly authorized what the Courts have always regarded as a fraud on the public seems to me so obviously wrong that I am tempted to dispose of this argument by adopting the words of Lindley L J, in *Edwards v. Dennis,* (1885) 30 Ch D. 454 at page 476: "That construction of the Act seems so irrational that I cannot adopt it".

22 This contention is based upon an assumption that Parliament must be presumed to have intended to change the law in a substantial way. This is not necessarily so. Compare section 21 of the *Interpretation Act,* R S C. 1952, chapter 158. Compare also the effect attributed by the Courts to section 14 of chapter 22 of the Statutes of 1879—see footnote #33. For purposes of this case, I do not need to explore the possible uses of a trade mark under the Canadian Act where there are two or more companies under a common control and carrying on connected businesses One view, and the one on which the plaintiff obviously had to insist, is that a trade mark must be used only to distinguish goods of the owner of the trade mark and it is infringement to use it on goods of a closely related company (even the parent of the owner of the trade mark). It would be consistent with this view to permit joint ownership and registration (under the *Interpretation Act,* the singular includes the plural) of a trade mark so that it could then be used to distinguish the goods of the owners One such possibility that I do not need to consider is whether a trade mark as defined by the present Canadian statute, which was first enacted in 1953, can be adapted to the concept of a "single organization" such as conceived of by Angers J. in the *Good Humour* case, [1937] Ex. C R. 61 at page 74 (unless, indeed, there is a partnership, in which event presumably the registration should be in the name of the partnership). Another unexplored area that I can avoid considering in this case is the "commercial

The *Trade Marks Act* was intended, as I read it, to be a code of law relating to trade marks in Canada (whether or not it is exhaustive of the common law, I need not consider). It is therefore a statute to which the principles enunciated by Lord Herschell in *Bank of England v. Vagliano* apply.[23] In deciding what any portion of the Act means, therefore, "the proper course is in the first instance to examine the language of the statute and to ask what is its natural meaning, uninfluenced by any considerations derived from the previous state of the law, and not to start with inquiring how the law previously stood, and then, assuming that it was probably intended to leave it unaltered, to see if the words of the enactment will bear an interpretation in conformity with this view". As Lord Herschell points out, resort may of course be had to the previous state of the law for the purpose of aiding in the construction of the code where there is some reason for it, for example,

(a) where a provision is "of doubtful import", and

(b) where, in the code, words are found that had previously acquired a technical meaning, or had been used in a sense other than their ordinary sense (in which event the same interpretation might well be put upon them in the code).

Lord Herschell emphasized that the first step taken should be to interpret the language of the statute, and that an appeal to earlier decisions can only be justified on some special ground.[24]

Applying these principles to the construction of section 47 of the *Trade Marks Act,* as a part of the statutory scheme or code created by that Act, I find, as far as the

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sense" of "proprietorship" of a trade mark and of the business in which it is used to which Duff J. (as he then was) made passing reference in *The Bayer* case, [1924] S C.R. 558 at page 584. Either of these approaches would serve only to negative the plaintiff's case as they both envisage a group ownership or right to use the trade mark which would be inconsistent with the idea of infringement by using the trade mark on the goods of one member of the group when it is registered in the name of another member.

23 [1891] A.C. 107 at pages 144-5.

24 See also *Robinson v. Canadian Pacific Railway,* [1892] A.C. 481, *Quebec Railway, Light, Heat and Power Company, Limited v. Vandry,* [1920] A.C. 662, and *S. & S. Industries Inc. v. Rowell* 56 D L R. (2d) 501 per Martland J. at p. 505.

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problems raised by this case are concerned, no such doubt as to the effect of the statute as might require resort to the previous law; and while words are employed that have a long history in the law of trade marks, their meaning is reasonably clear when they are considered in relation to the facts of the business and commercial world, without resort to earlier decisions.

Confining myself to the provisions of the statute *in so far as they are relevant to the facts of this case,* I can explain how I understand them as follows:

1. Section 2(*t*)(i) defines the particular kind of trade mark with which we are concerned. It is a "mark" that is used by a person for the purpose of distinguishing or so as to distinguish wares manufactured or sold by him from those manufactured or sold by others.

2. Sections 29 to 39 provide a procedure whereby a person who uses, or has commenced to use, a trade mark may obtain its registration in the register provided for by section 26.

3. Section 19 provides that the "registration" of a trade mark in respect of certain wares, unless shown to be invalid, gives to the owner the exclusive right to the use throughout Canada of such trade mark in respect of such wares.

4. Section 47 provides that a registered trade mark is transferable.

5. Section 18(1)(*b*) provides that the "registration" of a trade mark is invalid if the trade mark is not "distinctive" at the time proceedings bringing the validity of the registration into question are commenced; and "distinctive" in relation to a trade mark is defined by *section 2(f)* to mean a trade mark that "actually distinguishes" the wares in association with which it is used *by its owner* from the wares of *others.*

Leaving aside all the many aspects of the Act that have no bearing on the problem raised by this case, the language of the statute quite clearly, as I read it, contemplates a registered trade mark which is *used* (sections 2(*t*)(i) and 39) to distinguish the owner's goods from the goods of others and which is invalid unless it "actually distinguishes" the owner's goods from the goods of others (sections 2(*f*) and 18(1)(*b*)); and it contemplates that such a registered trade mark may be transferred either with or without the goodwill of the business in which it is being or has been used. The effect of a transfer of a trade mark is obviously,

(a) that the transferor, the former owner, immediately ceases to have any right to use the trade mark to distinguish *his* goods because the *exclusive* right has, by virtue of sections 19 and 47, become vested in the transferee; and

(b) the *exclusive* right to use the trade mark in respect of the goods for which it was registered becomes vested in the transferee.[25]

It does not, however, take much thought to realize that this exclusive right that has become vested in the transferee is a right to use the mark as a "trade mark" and not a right to use it for any other purpose; and a right to use it as a trade mark is a right to use it for the purpose of distinguishing or so as to distinguish the owner's wares from the wares of others.[26] (Any use by the owner that would have the inevitable effect of making the purchasing public think that his wares and the wares of some other person are the wares of the same person would be quite outside the exclusive right vested in him by the transfer—compare sections 16 and 6.) Furthermore, the exclusive right vested in the transferee by the transfer is subject in his hands, as it was in the hands of the transferor, to the condition that the registration of the trade mark is invalid if, at the time of an attack by legal proceedings, it does not "actually distinguish" the owner's wares from the wares of others.

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[25] I am assuming that none of the common law limitations on the *validity* of a *transfer* of a trade mark are applicable to a transfer under section 47(1). (Compare *Pinto v. Badman,* (1891) 8 R.P.C. 181 per Fry, L.J. at pages 194-5.) I express no opinion as to whether a transfer would be void or invalid *per se* if made in such circumstances, for example, as to indicate an intention to use it as a fraud on the public. It is not necessary for me to decide that question in this case.

[26] A submission was made by counsel for the plaintiff that section 4 defines how a trade mark is to be used so as to comply with the requirement that it be used "for the purpose of distinguishing" wares of the owner in the definition of a trade mark. As I read section 4, it relates exclusively to the question as to when a trade mark is to be regarded as used "in association with wares" for the purposes of a provision where such expression is used as, for example, in section 5.

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All this seems to me to be perfectly clear from a reading of the statute. I do not find any provision of "doubtful import" that requires resort to the prior law as an aid to construction and, if there are any terms that might be regarded as having previously acquired a technical significance—e.g., "distinguishes"—resort to the common law decisions shows that their meaning in the common law cases is that which appears obvious on a reading of the statute unaided by such cases.

My conclusion is therefore that there is no need, applying the principles laid down by Lord Herschell in *Vagliano's* case, to resort to the history of the law of trade marks as an aid to the interpretation of section 47 and that there is nothing in section 47 or the remainder of the Act to warrant reading into that section the very important addition contended for by counsel for the plaintiff, having regard particularly for the substantial change in the concept of a trade mark as defined by the statute that such addition would involve.

There is, however, a decision that might be regarded as authority for the application of the rule in *Heydon's* case, 3 Co. Rep. 7a; 76 E.R. 637. See *Eastman Photographic Materials Company v. Comptroller-General,* [1898] A.C. 571, per Lord Halsbury L.C. at page 573.[27] While I have some doubt as to the applicability of this rule where there is such a careful and complete code of trade marks law as is found in our 1953 statute (because such a code so obviously, in my view, calls for the application of the rule in *Vagliano's* case), I propose to review the history of our trade marks law on the assumption that the rule as applied by Lord Halsbury in the *Photographic Materials* case is applicable.

In the latter case, at page 576, the rule is stated as being that it is not only legitimate but highly convenient to refer

(a) to the former Act,

(b) to the ascertained evils to which the former Act had given rise, and

[27] An attempt was made by counsel for the plaintiff during argument to refer the Court to a report of a Departmental Committee. I did not permit it because it was not shown that it was to be used for any proper purpose The above case must be read, in this connection, with *Assam Railways and Trading Co., Ltd. v. C.I R.,* [1935] A.C 445

(c) to the later Act which provided the remedy.

What I now propose to do may appear to go further than is contemplated by the rule as so stated but, if the history of the legislation is to be used as an aid to interpretation, it would seem best to review it comprehensively.

At common law, apart from statute, trade marks have their origin in the tort of passing off. The fundamental rule was that no man has the right to put his goods up for sale as the goods of a rival trader. Using the trade marks with which the rival trader marked his wares to enable the purchasing public to distinguish them from those of others was one way of committing the tort of passing off. Gradually, this protection afforded to the user of a trade mark by way of the tort of passing off crystallized into the recognition of the trade mark as a property[28] belonging to the trader who had so used it that, in the minds of the purchasing public, it distinguished the wares to which he attached it from the wares to which it was not attached. Having regard to this function performed by a trade mark, the Courts felt constrained to hold, even when it became recognized as property, that its transferability was limited by its nature. Obviously, if, while a trade mark signified to the purchasing public the goods of A, it were transferred to B and B forthwith attached it to his goods and offered them to the purchasing public, it would, in the absence of special circumstances, signify to the public that the wares of B were the wares of A, which would be a misrepresentation and would be therefore, in a certain sense, a fraud on the public. The common law only recognized one exception to the rule against transferring trade marks and that was the case where the transferee took over the transferor's business in which event the use by the transferee of the trade mark that had been employed by his predecessor in the business would "according to the ordinary usages of the trade"[29] be understood by the purchasing public as saying no more than that he was carrying on the same business as his predecessor had formerly carried on. In such a case, as

[28] *The Leather Cloth Company, Limited v. The American Leather Cloth Company, Limited,* (1863) 4 De G J. & S. 136 per Lord Westbury, L.C. and (1885) 11 H.L.C. 523 (H L); *Singer Manufacturing Company v. Loog,* (1882) 8 A.C. 15, per Lord Blackburn at pages 29 *et seq.*; *Somerville v. Schembri,* (1887) 12 A.C. 453.

[29] *The Leather Goods* case, (1865) 11 H L C, 523 per Lord Cranworth at pages 534-5 and per Lord Kingsdown at page 542.

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Lord Cranworth said in the *Leather Goods* case, there was nothing to make it improper for the purchaser to use the old trade marks, as they would, in such a case, "indicate only that the goods so marked were made at the manufactory which he had purchased".[29] To this exception itself there was an exception in the case where the trade mark signified something to the public that could only be true when attached to the goods of the original owner of the trade mark, for example, a mark that signified the works of a famous artist.[30]

The significant point to be recorded in this review of the common law is that the common law not only visited a trade mark that was so used as to mislead or confuse the public (that is, a trade mark that had ceased actually to distinguish the goods of the owner) with invalidity, but it refused to recognize the validity of a transfer of a trade mark not made in connection with a limited class of change of ownership of business regardless of whether the transferee could use the trade mark so as not to mislead or confuse the public. In other words, in addition to regarding *a trade mark* as invalid (i.e., as having become *publici juris*) when it ceased to perform its function of distinguishing the owner's wares in the minds of the purchasing public,[31] the common law regarded *a transfer of a trade mark* as invalid except in the particular case where it accompanied a transfer of a business in which it could continue to be used without misleading or confusing the purchasing public.[32]

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[30] *The Leather Goods* case, (1865) 11 H.L.C., per Lord Kingsdown at pages 544-5: "Though a man may have a property in a trade mark, in the sense of having a right to exclude any other trader from the use of it in selling the same description of goods, it does not follow that he can in all cases give another person a right to use it, or to use his name. If an artist or an artisan has acquired by his personal skill and ability a reputation which gives to his works in the market a higher value than those of other artists or artisans, he cannot give any other persons the right to affix his name or mark to their goods because he cannot give to them the right to practise a fraud upon the public". (The underlining is mine.) See also *Bury v. Bedford,* [1864] 4 De G. J. & S., 351 at page 368.

[31] See, for example, *Ford v. Foster,* [1872] L.R. 7 Ch. A. 611, per Sir G. Mellish, L.J., at page 628.

[32] See *Pinto v. Badman,* (1891) 8 R.P.C. 181, per Fry, L.J. at pages 194-5: "Therefore, I conceive that that is the limit of the assignability of trade mark. It can be assigned, if it is indicative of origin, when the origin is assigned with it. It cannot be assigned when it is divorced from its place of origin, or when, in the hands of the transferee, it would indicate something different to what it indicated in the hands of the transferor".

From 1883 until 1938, this rule was reflected in the statute law of the United Kingdom concerning the registration of trade marks, which specifically provided that a trade mark, when registered, could be assigned only in connection with the goodwill of the business concerned.[33]

In Canada, on the other hand, a registered mark was, by statute, "assignable in law". See section 14 of chapter 22 of the Statutes of 1879. This was the statutory state of the law (see, for example, section 15 of R.S.C. 1927, c. 201) until 1932; but it would seem that the Courts read into it, by implication, the common law requirement that the assignment accompany a change in ownership of the goodwill of the business.[34] In 1932, this was spelled out in section 44(2) of *The Unfair Competition Act*, 1932, chapter 38, of the Statutes of 1932, and, as such, continued as part of the statute law of Canada until the present statute was enacted in 1953.

A parallel development in the law of trade marks is the principle applied to the licensing of the use of trade marks by someone other than the owner. The law has been summarized succinctly by Mr. Fox in his textbook on the subject as follows:

> A licence to use a trade mark was considered unnecessary if the mark was to be used in connection with the goods of the proprietor of the trade mark, and as illegal because leading to deception if it was to be used in connection with the goods of anyone else. (2nd ed., Vol. 1, p. 387)

Here again the principle of the common law was the logical development of the legal character of a trade mark as a mark to distinguish the goods of the owner from the goods of others. Just as the purchasing public would be misled or confused, in the ordinary case, if a transferee of title to a trade mark used it on his goods at a time when it signified to the public the goods of the transferor, so the purchasing public would be misled or confused if a licensee

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[33] Section 2 of *The Trade Marks Registration Act*, 1875, Section 70 of the *Patents, Designs and Trade Marks Act*, 1883, and Section 22 of the *Trade Marks Act*, 1905.

[34] Compare *The Bayer Co. v. American Druggist Syndicate*, [1924] S.C.R. 558, per Duff J. at page 583, and *Great Atlantic and Pacific Tea Company v. The Registrar*, [1945] Ex. C.R. 233, per Thorson P. at page 237. See also Annotation by Russel S. Smart [1923] 4 D.L.R. 555.

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used a trade mark on his goods at a time when it signified to the public the goods of the owner of the trade mark.[35]

It goes without saying that many attempts at transfers of trade marks and of licensing their use have run foul of these limitations on such activities. In some cases, such transfers or licenses have been bad because they resulted in deception or confusion of the public. In some cases they have been held bad simply because of the legal bar to the particular transfer or licence. Where the latter has been the case there has, presumably, been a feeling of grievance because the desires of this particular class of property owner have been frustrated by purely technical rules for no good reason. Such unnecessary interference with an owner in disposing of or using a trade mark is the only thing that I have been able to discover in my review of this branch of the law that might be regarded as an "ascertained evil" for the purpose of the rule in *Heydon's* case.

The new 1938 legislation in the United Kingdom endeavoured to meet this particular point of view by section 22 of the *Trade Marks Act,* 1938, which reads in part as follows:

> 22. (1) Notwithstanding any rule of law or equity to the contrary, a registered trade mark shall be, and shall be deemed always to have been, assignable and transmissible either in connection with the goodwill of a business or not.
>
> (2) A registered trade mark shall be, and shall be deemed always to have been, assignable and transmissible in respect either of all the goods in respect of which it is registered, or was registered, as the case may be, or of some (but not all) of those goods.
>
> . . .
>
> (7) Where an assignment in respect of any goods of a trade mark that is at the time of the assignment used in a business in those goods is made, on or after the appointed day, otherwise than in connection with the goodwill of that business, the assignment shall not take effect until the following requirements have been

[35] The *Trade Marks Act,* which came into force in 1953, provides for a very special type of licensee called a "registered user" subject to safeguards to protect the public interest. See section 49.

satisfied, that is to say, the assignee must, not later than the expiration of six months from the date on which the assignment is made or within such extended period, if any, as the Registrar may allow, apply to him for directions with respect to the advertisement of the assignment, and must advertise it in such form and manner and within such period as the Registrar may direct.

(8) Any decision of the Registrar under this section shall be subject to appeal to the Court.

The scheme of this United Kingdom legislation seems to be to provide for assignment in the case of *registered* trade marks, as follows:

(a) an assignment of a trade mark in connection with the goodwill of a business is unfettered just as it was under the previous law,

(b) an assignment of a trade mark that is not being used in any business at the time of the assignment is unfettered, and

(c) an assignment of a trade mark that is at the time of the assignment used in a business otherwise than in connection with the goodwill of that business cannot take effect until the fact of the assignment has been communicated to the purchasing public in such a manner as, in the view of the Registrar or the Court, the circumstances of the particular case require in order to protect the public from deception or confusion. (I am inferring here what, as seems obvious to me, is the duty of the Registrar under section 22(7)).

Certainly, I find no indication in this provision that it was intended by the United Kingdom Parliament to allow a transferee to use a trade mark in association with his goods even though it would indicate to the purchasing public that they were the goods of the transferor.[36]

[36] In *R.J. Reuter Coy. Ltd. v. Mulhens*, (1953) 70 R.P.C. 235, Evershed, M.R., referring to this provision, said at page 251: "...in my judgment it is now clear that...a mark may be validly assigned by one manufacturer to another without any assignment of the business or goodwill of the assignor, and so as thenceforth to be distinctive of a manufacturing origin different in fact from the previous manufacturing origin, so long, at any rate, as the mark is not deceptive." (The underlining is mine.)

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This is the background—sketched in broad outline only—against which subsection (1) of section 47 of the Canadian *Trade Marks Act* was enacted in 1953. It reads:

> 47. (1) A trade mark, whether registered or unregistered, is transferable, and deemed always to have been transferable, either in connection with or separately from the goodwill of the business and in respect of either all or some of the wares or services in association with which it has been used.
>
> . . .

Applying the rule in *Heydon's* case, in my view the position is that, under the *Unfair Competition Act,* immediately before the present law came into force, a trade mark could not be transferred except with the goodwill of the business in which it was used. This resulted in a transfer being held to be invalid even in a case where it was at least arguable that it could be used by the transferee as a trade mark to distinguish his goods from the goods of others without misleading or confusing the public.[37] I cannot assume that Parliament accepted it as an evil to be legislated against—indeed, I cannot believe that anybody put it forward as such an evil—that, under the previous statute, transfers were not allowed to operate so as to permit the use of trade marks to mislead or confuse the public. I can only assume that when Parliament adopted the new provision in the 1953 Canadian statute, it did so on the view that it was not necessary to have a public official or the Court dictate to a transferee how he is to educate the

[37] That a change in public understanding as to the significance of a particular trade mark is possible is illustrated by ***Bourjois & Co. v. Katzel,*** 260 U.S. 689 (1923) where, as appears from the judgment delivered by Mr. Justice Holmes, a trade mark of a foreign manufacturer came to indicate, after it was assigned to a United States distributor, "by public understanding, that the goods come from the plaintiff although not made by it." Whether or not the state of the law as reflected by such decisions as ***In re Apollinaris Company's Trade-Marks,*** [1891] 2 Ch 186, ***Lacteosote Limited v. Alberman,*** 44 R.P.C. 211, ***Impex Electrical Ld. v. Weinbaum,*** 44 R P.C. 405, ***John Sinclair's Trade Mark,*** (1932) 49 R P C. 123, ***Robert Crean & Co v. Dobbs & Co***, [1930] S C R. 307, and ***The Great Atlantic & Pacific Tea Co. v. The Registrar of Trade Marks,*** [1945] Ex. C R. 233, constituted an "evil" against which section 47 of the Trade Marks Act was directed seems to me to be at least questionable. Probably, it depends upon how one formulates the "evil". That it was not possible to effect a transfer for the purpose of using a trade mark to distinguish the goods of the new owner from the goods of others was certainly a gap in the law. That it was not possible under the old law to effect a transfer as part of a scheme to lead the public to believe incorrectly that the goods of the new owner come from the same manufactory as the goods previously marketed under the same trade mark cannot conceivably have been regarded as an "evil". It is only, however, if this latter formulation be regarded as the "evil" against which Parliament was legislating when it enacted section 47, that there is any substance in the argument of the plaintiff as to the effect of section 47.

public as to a change in ownership of a trade mark that has been transferred—as the United Kingdom Act contemplates by section 22(7) and (8)—because section 18(1)(*b*) read with section 2(*f*) of our Act operates as an automatic sanction to ensure that the transferee does not permit the trade mark to be used, after it has been transferred, as an instrument for deceiving or confusing the purchasing public.

For the above reasons,[38] the protracted nature of which I regret, I reject the submission of counsel for the plaintiff that subsection (1) of section 47 must be read as implying, as a matter of law, that any use by the transferee of a transferred trade mark actually distinguishes his goods from the goods of others whether or not such use does so in fact.

The plaintiff put forward an alternative argument based on subsection (2) of section 47 of the *Trade Marks Act* of 1953, which reads as follows:

> (2) Nothing in subsection (1) prevents a trade mark from being held not to be distinctive if as a result of a transfer thereof there subsisted rights in two or more persons to the use of confusing trade marks and such rights were exercised by such persons.

This provision should be read with section 15, subsection (1) of which reads as follows:

> 15. (1) Notwithstanding section 12 or 14, confusing trade marks are registrable if the applicant is the owner of all such trade marks, which shall be known as associated trade marks.

Subsection 15 authorizes confusing trade marks being registered in the name of the same person. Section 47(1) authorizes the transfer of one of them. As a result, if section 15 and section 47(1) are read literally, they authorize con-

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[38] It should not be overlooked that there is sufficient explanation for the wording of section 47(1) in the fact that the definition of trade mark in the 1953 Act extends to certification marks and proposed marks as well as marks that have gained some meaning in the market as to the origin of the goods. Furthermore, the rule in section 44(2) of the *Unfair Competition Act* was worded so as to invalidate assignments of a class permitted by such decisions as *Re Farina's Trade Marks,* (1881) 44 L.T n s. 99, *In re Wellcome's Trade-Mark,* (1886) 32 Ch.D. 213 and *In Re Greenlees' Trade Marks,* (1892) 9 R P C 93, where the assignments of the trade marks, while separate from the goodwill of the business, had the effect of uniting ownership of the trade mark and ownership of the goodwill of the business in which it had gained its reputation in the market. Such factors themselves, apart from any other explanation of the statutes, are sufficient answer to the contention that section 47(1) must be interpreted as impliedly authorizing the misleading or confusing of the public when such contention is based upon the view that there is no other explanation for the wording of the subsection that gives it any effect.

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fusing registered trade marks being owned by different persons. Subsection (2) of section 47 says that, if there should be a case where that did happen and "such rights were exercised by such persons", notwithstanding the express authority in section 15 for confusing trade marks, they may be held not to be distinctive. The plaintiff, however, says that, on the application of the maxim *expressio unius est exclusio alterius,* a transferred trade mark cannot be held not to be distinctive in any case not covered by section 47(2). In my view, having regard to the obvious purpose of section 47(2) and the very improbable result that, if that particular maxim is applied in the manner proposed by the plaintiff, Parliament intended to authorize, by implication, the deception of the public, the argument must be rejected. Where Parliament did intend to require that the use by some person other than the owner should be deemed by the Court to be use by the owner, it said so expressly (see section 49(3)) and provided safeguards for the protection of the public. See section 49(7), *Dubiner v. Cheerio Toys and Games Ltd.,*[39] per Noël J. at pages 541-2, *Heublein Inc. v. Continental Liqueurs Proprietary Ltd.,*[40] and *"Bostitch" Trade Mark,*[41] per Lloyd-Jacob J. at page 195.

My conclusion is, therefore, that the registrations of the trade marks in question are invalid. The defendant may move for judgment in accordance with that finding at some time convenient to all concerned.

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[39] [1965] Ex. C.R. 524.

[40] [103] C.L.R. 435.

[41] [1963] R.P.C. 183.

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I have, to the best of my ability, done justice to the arguments made to me in this case. These have not included any reference to the concluding words of section 2(*f*), which reads as follows:

> (*f*) "distinctive" in relation to a trade mark means a trade mark that actually distinguishes the wares or services in association with which it is used by its owner from the wares or services of others or is adapted so to distinguish them;

No attempt was made to relate the concluding words of this paragraph "or is adapted so to distinguish them" to the words in section 2(*m*) of the *Unfair Competition Act* "adapted to distinguish particular wares falling within a general category from other wares falling within the same category". It seems obvious to me that there can be no more than a superficial relationship.

The words in section 2(*f*) of the present Act relate to whether a particular trade mark is, as a matter of fact, at a particular time "distinctive". It is not a question as to whether a mark falls within a concept of "trade mark".

Obviously, a trade mark is distinctive in fact if it actually distinguishes. However, that would be an unrealistic requirement for the validity of a mark that has only recently been put into use. In such a case, it is sufficient, reading the latter part of section 2(*f*), if the trade mark is "adapted so to distinguish them"—that is, is adapted so as actually to distinguish the wares in association with which it is used by its owner from the wares of others. Whether it is so adapted cannot be decided, in my view, by reference only to the mark itself. It must depend also upon the meaning that such mark will have when used for the particular market.

Ottawa 1967

Apr. 24-28 May 1, 2

May 12

BETWEEN:

LYLE E. BRANCHFLOWER .... PLAINTIFF;

AND

AKSHUN MANUFACTURING COMPANY and V. & S. MACHINE COMPANY INC. .... DEFENDANTS.

Patent—Patent Act, R.S.C. 1952, c. 203—Subsection (8) of section 45—Ice removing blades for use in flake ice making machines.

In this conflict proceeding under subsection (8) of section 46 of the *Patent Act*, R S C. 1952, c. 203, as amended, to determine the respective rights of the parties on applications for a patent or patents containing claims numbered in this action C-1 and C-4, the subject matter was ice removing blades for use in flake ice making machines.

Held, (1) That the plaintiff's and defendants' respective applications for patents in this matter were directed to two different and distinguishable ice removing blades;

(2) That the ice removing blades described in the plaintiff's application for patent contained the elements described in claim C-4, and the defendants' does not; and that the plaintiff invented the design of the blades which has the elements prescribed in all the words in conflict claim C-1 and the defendants' does not;

(3) That the plaintiff made and disclosed the invention within the principles of *Christiani and Nielsen v. Rice* [1930] S.C R. 443 and the plaintiff formulated his inventions empirically within the principles of *Scragg & Sons Ltd. v. Leesona Corporation* [1964] Ex. C R. 649.

(4) That the plaintiff is entitled to costs.

CONFLICT PROCEEDING under *Patent Act.*

W. R. Meredith, Q.C. and *D. M. Finlayson* for plaintiff.

James A. Devenny and *N. Fyfe* for defendants.

GIBSON J.:—This is a conflict proceeding under subsection (8) of section 45 of the *Patent Act,* R.S.C. 1952, c. 203 as amended, to determine the respective rights of the parties on their applications of a patent or patents containing claims which are numbered in this action C-1 and C-4.

The plaintiff resides at Seattle, Washington and is the owner of Canadian patent application 626,587 filed February 7, 1952 (Ex. P-1).

The defendant, V. & S. Machine Company Inc., is a State of Illinois corporation and is the owner of Canadian patent application 616,890 filed July 14, 1951 (Ex. F), being the assignee of it from the defendant Akshun Manufacturing Company, another State of Illinois corporation (see Ex. N), which in turn was the assignee from the alleged inventor, one Gerald M. Lees (see Ex. M).

Both the plaintiff's and the defendants' applications each describe flake ice making machines to make sub-cooled flake ice. Nothing in either application, including the claims, however, apart from the reference to the blades for removing ice (sometimes referred to as knives, cutters, sweepers, etc.) was not known to persons skilled in the art prior to the beginning of 1949.

Both the plaintiff and the defendants filed applications for patents in the United States and each were issued a patent. The plaintiff's United States patent contains a claim similar in wording to claim C-1 in this action and a claim practically similar in wording to claim C-4, the only difference being in the words of the last phrase thereof.

The relevant dates of filing in the Canadian and United States patent offices of plaintiff and defendants are as follows:

February 8, 1951—The plaintiff, Branchflower, filed U.S. application for patent, serial number 210,030 (Ex. P-3) resulting in U.S. patent No. 2,735,275 (Ex. P-4)

February 7, 1952—The plaintiff, Branchflower, filed Canadian application serial number 626,587 (Ex. P-1)

April 9, 1951—The defendants' assignor, Lees, filed U.S. application for patent, serial number 220,044 (Ex. R) resulting in U.S. patent no. 2,716,869 (Ex. S)

June 14, 1951—The defendants' application was filed in Canada, serial number 616,890 (Ex. F); a duplicate of Ex. R above.

The decision of the Commissioner of Patents in this matter was made on August 13, 1959 by which he awarded conflict claim C-4 to the plaintiff and conflict claim C-1 to the defendants.

On November 5, 1959 the plaintiff instituted this action claiming that conflict claim C-1 should also have been awarded to him and the defendants deny this and by counter-claim claim that conflict claim C-4 should also have been awarded to them.

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Conflict claims C-1 and C-4 read as follows:

C-1

A flake ice maker and removing device comprising a vertical cylindrical shell member open at the bottom and having an inner surface; refrigerating means refrigerating the said inner surface so that water deposited thereon will form into ice; water supply means depositing water on said inner surface; a driven member coaxially mounted of and in said cylinder; a plurality of axially spaced apart ice removing blades carried by said driven member, each having an outer arcuate ice engaging edge portion disposed generally in a horizontal plane, and in close proximity to said inner surface, whereby ice forming on said inner wall is removed at a plurality of locations; and a water collecting trough at the lower edge of said inner surface.

C-4

A machine for the manufacture of flake ice, comprising: a cylindrical shell having an inner surface adapted to be refrigerated; means for supplying water to said surface so that ice in sheet form may be formed thereon; rotatable means arranged coaxially of said shell; base means extending axially of and secured to said rotatable means; axially spaced apart ice removing blades secured to said base means adjacent to said inner surface, each of said blades having a face normal to said surface, and said face being at an angle to the plane of its rotation, and with the leading portion thereof at a higher elevation than the trailing portion.

Flake ice, the product of the machines in both the plaintiff's and the defendants' said applications, is ice in the form of small relatively thin pieces, ragged edged, as distinguished from being in block or cube form. Flake ice is typically of reasonably uniform thickness of approximately $\frac{1}{8}$ inch. Its other dimensions are irregular but it is ordinarily no more than $\frac{1}{2}$ inch across in any other dimension. The general appearance of a single piece of flake ice is not unlike a tiny reasonably regular piece of broken window glass.

Flake ice is also sub-cooled, usually to a temperature of from 0 degrees to 20 degrees above F.

Flake ice has many uses, but very important uses have been and are in the fishing and poultry industries. It is particularly desirable for these purposes because flake ice provides a very large area for cooling per unit of weight, much greater than any other commonly used form of ice such as blocks, cubes or crushed ice.

Flake ice is preferred for the fishing industry over cube ice or crushed ice for additional reasons other than its large surface area. To be useful in the fishing industry, ice must be of sufficiently small particle sizes so that it can be easily packed in the fish carcass. Flake ice does not have strong sharp edges or lumps which might tear the fish flesh. Flake ice put to this use, being sub-cooled, will not pack into a solid mass in storage, which would make it difficult to handle. Flake ice is very satisfactory in all aspects mentioned and is in great demand for the fishing industry; and also the poultry industry.

There was nothing new about flake ice in 1949. It had been made and used for decades. It had been made by causing water to freeze on a smooth surface and then by some mechanical means was broken off into small pieces.

Both applications for patent herein use this method.

Both applications also relate to making ice on the inside of a rotary drum and then taking it off by blades (sometimes called knives, cutters, sweepers, etc.) causing it to fall to the bottom of the drum as flake ice.

In 1949 there also was nothing new in the refrigeration equipment used to freeze.

Both applications relate to essentially the same matter.

And as stated, all other components of the ice machines in both applications were part of the prior art in 1949.

What is in issue in these proceedings is the assertion of each inventor that he invented the blades, (sometimes called knives, cutters, sweepers, etc.) for removing the ice in an ice removing machine producing flake ice, containing all the elements described in conflict claims C-1 and C-4. Each claims to have made the inventive break-through.

Ernest H. Sinclair, a consulting engineer in Toronto, called as a witness by the plaintiff, puts it this way:

> In summary, it was known to produce the known substance flake ice by applying water to the inside or outside of a refrigerated drum, and it was also known to remove the ice by various kinds of cutters or blades. Any improvement making use of the features just referred to would have to have involved particular new and useful design of one or more of such features.
>
> What was desired to be achieved by a flake ice making machine was known. It was known that machines for producing flake ice should ideally produce dry, subcooled, friable, discrete flakes of ice of large surface area in relation to weight.[1]

The plaintiff's submission in brief is this: Conflict claims C-1 and C-4 are drawn in sufficiently broad language that

[1] Ex. P-12, pp. 13-4.

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they describe each of the plaintiff's and defendants' machines except for the cutting blades (sometimes called knives, cutters, sweepers, etc.) and that the only matter in issue is the design of the respective blades of the parties; that the plaintiff in designing and fabricating his blades invented the subject matter of claims C-1 and C-4; that the defendants (Lees) in designing and fabricating, or in describing its blades, did not; provided, however, that the plaintiff does not say that the defendants (Lees) did not make any invention, but instead says that Lees made another and different invention not containing the elements described in claims C-1 or C-4; and that the plaintiff alleges a date of invention not later than July 31, 1950.

The defendants' submission in brief is this: That the cutting blades (sometimes called knives, cutters, sweepers, etc.) such as filed as Ex. P-20 at this trial which the parties agree is a blade invented by Lees and designed by him sometime in July or August, 1949, is within the concept of claim C-1; that the plaintiff's alleged invention is not; that claim C-4 is inoperative or (conceding that the blade Ex. P-20 does not contain the elements described in claim C-4) it is within Lees' concept of invention on a so-called two-faced theory (see p. 102 of Ex. I, Note Book of Lees); that the plaintiff's alleged invention is not within the concept of claim C-4; and that the defendants allege a date of invention of July or August, 1949.

At the time of this trial, the plaintiff, the alleged inventor of the invention in his application, was too sick to testify; and the defendants' alleged inventor, Lees, was dead.

Part of the plaintiff's evidence was that the licencee under its United States patent, containing essentially claims C-1 and C-4, North Star Ice Equipment Co. Inc., employing the concept of the plaintiff's alleged invention of his blades, had manufactured and sold over 1,000 machines in the world market, 300 of which had been sold in Canada.

The defendants, on the other hand, adduced no credible evidence that any machine incorporating the Lees invention of blades Ex. P-20, was ever sold commercially.

The plaintiff's witnesses were: Mr. Ernest H. Sinclair, mechanical engineer, Toronto, Ontario; Mr. Allan J.

Treuer, President of North Star Ice Equipment Co. Inc., and former partner with the plaintiff in the firm known as Lyle E. Branchflower and Company, Seattle, Washington; Mr. Meryl H. Jenkins, production superintendent in 1949 and 1950 and now, of Lyle E. Branchflower and Company; Mr. Paul Blivene, a patent attorney, formerly of Seattle, Washington, who in 1950 was retained by the plaintiff to prepare and file his application for a United States patent.

The defendants' witnesses were: John E. Watkins, mechanical engineer of Maywood, Illinois; James Albright, President of both the defendant Companies; Lew E. Flanders, a general attorney at law, Seattle, Washington.

The plaintiff by letter agreement dated May 3, 1949 (Ex. D) hired the said Gerald M. Lees, the defendants' alleged inventor, to construct an ice machine and for this purpose to prepare shop drawings in consultation with the foreman of Lyle E. Branchflower, one Charles Nelson, for the production of a unit which should produce approximately ten tons of flake ice per 24 hour day. The agreement provided among other things as follows:

> . . . For your technical knowledge and preparation of drawings, supervision of assembly, and starting of the operation of the unit, we will pay you at the rate of $100 00 per week for the 6 week's period. When the unit has been put into operation, we will then pay you the $400 00, or total of $1,000 00 for the engineering, design, and supervision of construction of this unit.
>
> It is further understood that you will design and supervise construction of additional units on the basis of $500.00 per unit, if we so desire.
>
> The preparation of the drawings will be done in your residence. Fabrication and production of the various units for the machine will be contracted for by us and all costs will be paid by us The assembly of the machine will be in our own shop.[2]

Lees' employment terminated on August 18, 1949 after a disagreement.

At least by August 18, 1949 a so-called experimental machine had been fabricated and was working at the premises of Lyle E. Branchflower and Company. The blades in it designed by Lees were similar to the blades Ex. P-20 which the plaintiff agrees is a blade invented by Lees.

Prior to this employment of Lees by the plaintiff, namely, on April 19, 1949, Lees attended the law office of Lew E.

[2] Ex D

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Flanders, the said attorney at Seattle, Washington, for the purpose of having pages 100, 101, 102 and 103 of a Note Book of his, alleged to be a record of his invention for an ice making machine, notarized. This Note Book is Ex. I. Mr. Flanders affixed his signature as a Notary Public and his notarial seal on said pages on April 19, 1949.

Page 100 dated March 25, 1949[3] reads in part:

> A way to make a large ice machine. . . . Run two sets of knives, one set for each plate (essentially Lessard-Lees knife assy) . . .

At page 102 dated March 27, 1949[4] there appear these words:

> An efficient knife for flat surface. . . . It seems to me that if I could make a thin cut nearly thru the ice sheet & then start driving the wedge to apply shear to the bond that this would be more efficient.

There then follows subject sketches of blades and opposite one appear these words: "Lay this off". This is alleged to mean curved.

Then under date March 29, 1949, page 102[5], there appears a sketch of a blade with a saw cut in it, the tail portion of which is bent down. These words appear under it:

> A good knife perhaps Use 20° (sharp) blade thruout apply shear by making a saw cut & bending tail end of blade down to bear down on ice—"Split the log & then drive the wedge".

The evidence of the plaintiff, by the witness Treuer, is that the said experimental machine using blades similar to Ex. P-20 was not satisfactory because it did not remove substantially all the ice and would not run for long periods unattended, among other things; and that as a consequence, the plaintiff continued to experiment with the design of blades to produce a more satisfactory ice cutting machine. I accept this evidence.

Treuer testified that not later than July 31, 1950, the plaintiff had designed and had caused to have fabricated blades in an ice making machine which produced the successful results sought. Ex. P-29 is part of a rail containing eight blades, all of which are examples of such blades. Mr. Treuer says the plaintiff disclosed this to him, to Charles Nelson who caused the actual fabricating of them, and to others in the plant of Lyle E. Branchflower.

[3-4-5] Ex. I

I accept this evidence and also infer that the milling along the bottom of such blades had been done by that time.

Treuer says the plaintiff gave these blades (Ex. P-29) to Mr. Blivene, the said patent attorney, on October 19, 1950, when the plaintiff retained the latter and authorized him to prepare a patent application. Mr. Blivene testified that he received Ex. P-29 and used it in preparing the United States patent application of the plaintiff. Mr. Blivene also testified that he made various inquiries of the plaintiff and of the employees at the plant of Lyle E. Branchflower to assure himself that there was no joint inventor of Ex. P-29. I accept this evidence.

The engineer, Sinclair, called by the plaintiff, said that he had seen machines working commercially which had blades in them incorporating the plaintiff's concept of blades exemplified by the blades on Ex. P-29. He said they were in machines made by North Star Ice Equipment Co. Inc. He identified Ex. P-31 and Ex. P-32 as examples of such North Star Ice Equipment Co. Inc. blades. He identified Ex. P-11-F, which is an enlarged version of figure 9 of a drawing of the plaintiff's blade in his said Canadian patent application.

Sinclair's affidavit as filed, complied with Rule 164B of this Court and also the Order of this Court dated December 14, 1966 concerning the conduct of this trial.

Watkins, the engineer who gave evidence on behalf of the defendants, had never seen a machine working which he identified as using North Star blades implementing the alleged invention of the plaintiff exemplified by the blades in Ex. P-29; and also had never seen a flake ice machine operating which had in its blades employing the Lees concept of blade as exemplified by the blade Ex. P-20.

An affidavit of Watkins was filed purporting to comply with Rule 164B of this Court, but it contained nothing which related to the provisions of the said Order of this Court dated December 14, 1966, that expert testimony at the trial could be adduced as to the technical significance of the words and phrases of claims C-1 and C-4.

Speaking generally, Sinclair's evidence, in my view, in the main is to be preferred to that of Watkins. His experience over thirty years and his technical training admirably

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qualified him to give the evidence he did, and his evidence including that adduced on cross-examination, I prefer where it conflicts in any way with that of Watkins on any material point. Watkins, in my view, was more advocate than witness.

Speaking generally also, Albright for the defendants was an unsatisfactory witness. He described himself, *inter alia,* as a promoter of patents. He was not truthful in respect to certain material evidence at this trial. From this, from his general demeanour, and from other *indicia,* I conclude I do not accept any of his evidence in so far as it is relevant to the determination of the issue of this action. Other facets of the unreliability of this witness were expressed by the plaintiff as far back as July 28, 1950. (See letter to the plaintiff from Albright dated July 28, 1950, which was put in evidence by the defendants as Ex. O.)

On the evidence, the issue for decision in so far as conflict claim C-1 is concerned, resolves itself into a question as to whether the plaintiff invented the design of the blades in the structure (Ex. P-29) and whether such design has the elements prescribed in these words in conflict claim C-1, namely: "each having an outer arcuate ice engaging edge portion disposed generally in a horizontal plane"; or whether the defendants' (Lees) invention of blade Ex. P-20 which it is agreed was invented in July or August, 1949, has the elements called for in those said words in conflict claim C-1.

On the evidence, the issue for decision in so far as conflict claim C-4 is concerned, is again whether the plaintiff invented the blades in the structure (Ex. P-29) and also whether they have the elements called for in these words in said claim, namely: "axially spaced apart ice removing blades secured to said base means adjacent to said inner surface, each of said blades having a face normal to said surface, and said face being at an angle to the plane of its rotation, and with the leading portion thereof at a higher elevation than the trailing portion."; or whether as contended by the defendants, claim C-4 is inoperative in that it does not describe the concepts of the blades on Ex. P-29 or Ex. P-20 (which the defendants concede) or alternatively, whether it describes the Lees invention of blade disclosed at page 102 of his Note Book (Ex. I) on a so-called two-face theory (which is discussed later in these reasons).

As to the wording of both claims, they should be interpreted, in my view, according to the ordinary dictionary meaning of same.

As to the above quoted relevant words in conflict claim C-1, I am of opinion that Sinclair in his said affidavit filed, and orally, adequately and correctly explains them, even though in employing the words he did, he had in mind in the main, the blades used in a North Star flake ice machine and the North Star ice machine generally. This does not detract from their validity. His words of description are:

> 12. (12) *"Outer arcuate ice engaging edge portion"*—The phrase altogether means a particular surface. This is the surface (portion) of the ice removing blade that actually comes into contact with the ice and exerts a downward force on the ice below the blade which breaks adherence to the drum wall. It is clear that in the apparatus shown in both of the patent applications set forth in paragraph 6[6] hereof, such surface is the lower surface of each blade. The drum wall is round and cylindrical and the outer extremity (edge) of the surface on the blade is curved (arcuate) to match the curvature of the drum wall. The ice removing blade is mounted on the driven arm so that its outer edge clears the drum wall by a very small clearance which I know from my experience in the industry to be about 0 005"; such dimension in practical terms is approximately equal to the thickness of a sheet of good bond paper. The underneath surface of the blade engages the ice, pushing the ice downward until the bond of the ice to the drum wall is broken. Thus the ice falls by gravity out of the machine into storage.
>
> (13) *"Disposed generally in a horizontal plane"*—Although these words have a broader general meaning, as applied to machines of the kind described in the patent applications set forth in paragraph 6 hereof, this phrase refers to the orientation or position of the ice engaging surface of the ice removing blades when

[6] 6. THAT I am aware that this action is concerned with a patent application of Lyle E. Branchflower, Serial No. 626,587 entitled "ICE MAKING MACHINE AND THE ART THEREOF" and a patent application of Gerald M. Lees, Serial No. 616,890, entitled "KNIVES FOR FLAKE ICE MAKING MACHINES", both of which applications I have read The opening words of the said Branchflower application state that it is concerned with "the making of sub-cooled ice in flake form" and the opening words of the said Lees application states that it is concerned with "an improved machine for making flake ice and a knife therefor". Assuming the quoted words in the last sentence are used in the sense that they are used as terms relating to refrigeration in the food processing industries, it is my opinion that both the said patent applications have to do with the manufacture of a particular form of ice known as flake ice.

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properly positioned in the ice making machine The drum wall, although round, is vertical or upright. If one placed one leg of a carpenter's square upright against the inside wall of the drum and the other leg toward the shaft in the center of the drum, the ice engaging surface of the ice removal blade would rest upon the inwardly extending leg of the carpenter's square. Thus, the working surface of the blade may be said to be generally in a horizontal plane.

(14) *"Outer arcuate ice engaging edge portion disposed generally in a horizontal plane"*—This phrase combines Nos. 12 and 13 phrases so the combined definition of Nos. 12 and 13 applies This phrase defines the placement and position of the working surface of the ice removal blades. The "edge portion" is the working surface on each blade. Its outer extremity is arcuate and in the Branchflower application referred to in paragraph 6 hereof, matches the curvature of the drum wall. This surface is generally horizontal in that it extends from the vertical wall inwardly toward the central shaft in a horizontal direction.[7]

2. THAT upon reviewing my said affidavit of March 21, 1967, it seems to me that a further comment will be helpful in understanding the facts deposed to Particularly in Paragraph 12(12) and 12(14) of my said affidavit I have referred to the term "arcuate edge portion", and I wish to point out that the expression "arcuate edge portion" is distinguishable from a structure which is "tangential" to the inner wall of the drum. "Tangential" implies a straight line which is a tangent to a circle and "arcuate edge portion" could therefore not be "oriented in a substantially tangential direction in relation to the inner wall".[8]

I agree with the opinion of Sinclair that the above quoted words of claim C-1 require that the ice removing blades have a working surface generally in a horizontal plane and that such surface be outer arcuate and ice engaging.

The blades of the plaintiff exemplified by Ex. P-29 clearly fulfil this requirement of structure in that, *inter alia,* it is arcuate along its full working surface and all of such surface gets into the ice (engages it). The Lees' blade exemplified by Ex. P-20 does not. It is outer arcuate only on the front part of it where it scores the ice and is not in the rear part so to speak, of its blade which wedges the ice off; and in consequence does not engage the ice along the whole of its working surface.

I also agree with Sinclair that to engage the ice is to be in the ice and not just touch it and such engaging must be in an ice removing functional part of the blade. As stated, the blades exemplified by Ex. P-29 fulfil this requirement and the blades exemplified by P-20 do not.

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[7] Ex. P-12 pp. 8-9.

[8] Ex. P-23.

As to the above quoted relevant words in conflict claim C-4, I am of the opinion that Sinclair adequately and correctly explains them. His words of description are:

12 (24) *"A face normal"*—Normal is another word for perpendicular. The drum inside surface is vertical and the lower surface (face) of the ice removal blade is generally horizontal. Vertical is usually thought of as perpendicular to horizontal and vice versa. Hence, the under surface or face of the ice removing blades may be said to be perpendicular or normal to the vertical surface of the drum on which the ice is formed.

(25) *"A face normal to said surface"*— The surface is the inside surface of the drum. The face is the underneath (lower) surface of the blades that remove the ice. These drum and blade surfaces are arranged in a perpendicular fashion relative to each other and may be described as normal to each other.

(26) *"Face being at an angle to the plane of its rotation"*—The face is the lower flat surface of the blade that removes the ice. This surface is about two inches long from front to back. The blades are carried around the interior of the drum but do not move up or down. The blades move past the drum, the ice on the drum wall being stationary because the drum is stationary.

The plane of rotation is the path in which each blade is carried and is horizontal since the blades move neither up or down in the machine. The flat underside surface of each blade is tilted slightly so that the rear part of the surface is lower than the front. As the surface (face) engages a given piece of ice below it on the drum wall, this tilted surface forces the ice downward until its bond or adherence to the drum wall is loosened and broken. The face of the blade urges the ice downwardly in a manner similar to the way a road grader blade pushes snow or gravel to the side as the machine travels along the road. Attached to this my affidavit and marked as Exhibit "G" is a brochure of Huber-Warco Company entitled "Motor Graders", which, particularly at page 12 thereof illustrates the same action just discussed.

(27) *"An angle to the plane of its rotation"*—This phrase is part of No. 12(26) above and the same definition applies. The blades are carried in a horizontal path in the machine. The working lower surface on each blade is tilted at an angle which in the Branchflower patent application set forth in paragraph 6 hereof is 4° or 5° to the plane of rotation in order to thrust the ice downwardly as the blades pass the ice clinging to the drum wall.

(28) *"The leading portion thereof"*—This refers to the working surface of the ice removal blades. The part that "leads" is in front of the rest of the blade determined by the direction of rotation of the blades in the drum. Most of the machines rotate the arm and thus the blades in counterclockwise direction viewed from above the machine.

(29) *"The leading portion thereof at a higher elevation than the trailing portion"*—The words describe the same relationship of the same parts as No. 12(26). "Portion" refers to the flat lower surface of the blade sometimes referred to as the "face" of the blade or that surface in contact with the ice. Each blade

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> being moved horizontally in a circle about the drum but neither moved up or down, the working surface on the blades is oriented relative to elevation in the ice making machine in order to define the slight tilt of the face relative to the horizontal. The slight tilt of the face means simply that the front end of the working surface is slightly higher than the rear end of the flat face. The face is a flat surface from front to rear.
>
> These words merely define the slight tilt of the working surface in technically accurate terms of relative elevation in the machine.
>
> (30) *"The trailing portion"*—The meaning of this expression is apparent from No. 12(29) just referred to.[9]

I am of opinion that the blades exemplified by Ex. P-29 embody all the elements contained in these words. The only submission made that they did not, was based on the fact that strictly speaking, geometrically the blade exemplified by Ex. P-29 does not have a face normal (perpendicular) to said surface (that is the inner surface of the cylindrical wall) because the ice engaging portion of such blade is in an inclined plane of about 5 degrees off horizontal. In my view, this language of the claim may be slightly inadequate if the words were left by themselves, but these words are qualified by the two phrases following which make it perfectly clear what is meant:

> . . .and said face being at an angle to the plane of its rotation, and with the leading portion thereof at a higher elevation than the trailing portion.[10]

As a result, I am of opinion that the blades exemplified by Ex. P-29 embody all the elements contained in the words of claim C-4.

The ice engaging surface on the Lees blade exemplified by Ex. P-20 is a bevelled surface at about 45 degrees to the drum wall and therefore clearly does not have a "face normal to said surface". It clearly does not embody the elements contained in claim C-4.

As to the defendants' submission that Lees' Note Book (Ex. I) at page 102 describes a blade embodying all the elements in the said key words of claim C-4 on the so-called two-faced theory, it is clear that such is without merit.

The two-faced theory in brief is that the blade sketched under the date March 29, 1949 in the said book has two parts, the leading portion being normal to the said surface

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[9] Ex. P-12 pp 11-3

[10] Claim C-4

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and the trailing portion namely, the saw cut or wing tail portion, being not. The submission of the defendants is that the leading portion is normal (or perpendicular) "to said surface" and this should qualify it as being within claim C-4, even though the saw cut or wing tail portion is not. Watkins in his affidavit (Ex. K) at paras. 14, 15 and 16 put this theory in this way:

> 14. Attached hereto and marked Exhibit "G" to this my affidavit are pages 100 to 103 of a notebook of Gerald M. Lees dated March 25-30, 1949. Page 102 of the said notebook is particularly relevant in that it includes various sketches of what are obviously ice-removal blades, called knives. The blade representation which is marked 1 in red would have taught or suggested to me in 1949 an ice-removal blade which in operation would be disposed in an ice-making machine (of the type referred to in paragraphs 10 and 12 hereinabove) generally in a horizontal plane, and which blade has an ice-engaging edge portion 1a which is arcuate in configuration.
>
> 15. The diagrams which have been marked 2 and 3 in red depict an ice-removal blade which would have taught or suggested to me in 1949 an ice-removal blade having a surface marked 2a in red, which surface could be described as a face which would be normal, that is at right angles, to the inner surface of a cylindrical shell when in operation, the said face 2a also being inclined at an angle to its plane of rotation so that the leading portion thereof is at a higher elevation than the trailing portion.
>
> 16. The said page 102 of Exhibit "G" also discusses the essence of this type of blade, namely the use of a relatively sharp leading edge which makes a "thin cut" in the ice and then is followed by an inclined surface which will shear off the ice. "Split the log and then drive the wedge".

I am of the opinion that no person skilled in the art reading these said words in claim C-4 would come to the conclusion that it suggested to him a blade designed along such two-faced theory; and therefore, such does not contain the elements described in claim C-4.

In summary, the plaintiff's and the defendants' application for patents in this matter, in my view, are directed to two different and distinguishable ice removing blades for use in flake ice making machines and I adopt the words of Sinclair which he employs in differentiating them:

> . . .the Lees' structure (involves) a two-part blade first scoring or grooving the ice and second working in the grooves on the ice for removal; the Branchflower structure being a single flat surface blade like a road grader blade; . . .[11]

[11] Ex. P-12, p. 22, para. 29

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In elaboration, in differentiating the Branchflower blade from the Lees blade, I also agree with the opinion of Sinclair that the Branchflower structure of blades operate on an auger-like principle and that the rotational effect causes the ice on the inside of the cylindrical surface of the ice machine to be swept in a continuous motion; that the sweeping off is caused by means of this auger-like action of the ice removing blades; that it is the underside that also does the shearing and that except for some minor wedging at the front of the blade which is inconsequential when it first comes in contact with the ice, that the shearing takes place in a manner which he aptly describes as like a road grader; and that using the analogy of an auger has its limitation like most analogies, especially when in referring to the milled underside of the blade in respect of which the analogy does not fit, but which failure to fit is of no consequence.

Finally, on the issue of whether the plaintiff made the invention in his application, the evidence in my view satisfies the burden of proof the plaintiff had.

That the plaintiff made and disclosed the invention within the principles of *Christiani and Neilsen v. Rice*[12], in my view, is proven by the evidence of Treuer and amply corroborated by the evidence of Jenkins and Blivene; and that he formulated the invention empirically within the principles of *Scragg & Sons Ltd. v. Leesona Corporation*[13] is established by the blades of Ex. P-29.

In the result therefore, I find that the plaintiff was the inventor of the elements contained in conflict claims C-1 and C-4 and that Lees was not the inventor; and that accordingly the plaintiff is entitled as against the defendants to the issue of a patent including claims C-1 and C-4 in conflict as applied for by him.

The plaintiff is also entitled to costs.

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[12] [1930] S.C.R. 443.

[13] [1964] Ex. C.R. 649

Toronto 1967 Sept. 18-22, 25-26.

Ottawa Dec. 14

BETWEEN:

CONN STAFFORD SMYTHE ....APPELLANT,

AND

THE MINISTER OF NATIONAL REVENUE .... RESPONDENT,

AND BETWEEN:

CONN SMYTHE ....APPELLANT,

AND

THE MINISTER OF NATIONAL REVENUE .... RESPONDENT,

AND BETWEEN:

CLARENCE H. DAY ....APPELLANT,

AND

THE MINISTER OF NATIONAL REVENUE .... RESPONDENT.

Income Tax Act, c. 148, R.S.C. 1952, sections 105-105B—Transactions "dividend stripping" or "surplus stripping"—"Daylight loan"—Applicability of section 137(2)—Not a "bona fide" transaction.

These appeals tried together on common evidence from re-assessments on income tax for the taxation year 1961 relate to the categorization of the receipts of monies received by the appellants as a result of series of transactions in December 1961 concerning the shares held by each of them in an Ontario corporation by the name of C. Smythe Limited. The series of transactions are sometimes referred to as "dividend stripping" or "surplus stripping".

In December 1961, C. Smythe Limited has undistributed earned surplus of approximately $728,652.

As a result of the series of transactions carried out in December 1961, this said undistributed earned surplus was paid or appropriated to the shareholders of C. Smythe Limited of which the appellants were three of them. This payment or appropriation was in the form of $275,336 cash and $423,316 worth of non-interest bearing debenture certificates in a newly incorporated company known as C. Smythe For Sand Limited.

The appellants contended that the receipts were capital receipts and not income.

There were no business reasons for entering into these transactions.

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The relevant transactions in the said series of transactions were as follows:

In December 1961, the appellants caused a new Ontario corporation to be incorporated under the name of C. Smythe For Sand Limited, of which they became the owners of the issued shares (which were common shares).

All assets of C. Smythe Limited were then transferred to C. Smythe For Sand Limited in exchange for a promissory note to the value thereof, *viz.* $2,611,769.

On December 28, 1961, all the shares of C. Smythe Limited were sold to F. H. Cameron Limited and Dabne Enterprises, two Vancouver based corporations, incorporated under the British Columbia *Companies Act*. To accomplish this, certain transactions were entered into practically simultaneously: the appellants caused a temporary loan to be made to C. Smythe For Sand Limited by the Toronto-Dominion Bank, Toronto Branch, in order to pay off the said promissory note to C. Smythe Limited, thereby putting its assets in cash form; and F. H. Cameron Limited and Dabne Enterprises Limited obtained a temporary loan—"daylight loan" from the Bank of Montreal, Vancouver, B.C., to pay the appellants and A. M. Boyd for their shares in C. Smythe Limited; F. H. Cameron Limited and Dabne Enterprises Limited (*qua* new and then only shareholders of C. Smythe Limited) caused C. Smythe Limited to invest in preferred shares of F. H. Cameron Limited and Dabne Enterprises Limited equal to the amount (i.e. $2,611,769) of its cash assets, thereby putting cash in F. H. Cameron Limited and Dabne Enterprises Limited to enable them to pay off their "daylight loan" from the Bank of Montreal; and the appellants subscribed and paid for certain common shares in C. Smythe For Sand Limited and loaned it certain monies, from the monies they received from this sale of their shares in C. Smythe Limited; and then the temporary loans were respectively repaid to the said banks by C. Smythe For Sand Limited and F. H. Cameron Limited and Dabne Enterprises Limited.

The net cash assets of C. Smythe Limited after this temporary bank loan was made, as stated, had a value of $2,611,769. The appellants and A. M. Boyd sold their shares for $2,570,336 or $41,433 less than the book value of these shares at the time.

The said sum of $41,433 was 5 per cent of $728,752. (The undistributed earned surplus of C. Smythe Limited) namely, $36,433 plus $5,000.

Held, that these payments or appropriations were income in the hands of the appellants and that section 137(2) of the *Income Tax Act* applied to the facts of these cases in that the "result" of these transactions was that a "benefit" was conferred on the appellants and the other shareholders of C. Smythe Limited by disposal of its assets and that person "who conferred this said 'benefit' was C. Smythe Limited" with the help of and as "parties thereto", the following and others, namely, F. H. Cameron Limited, Dabne Enterprises Limited, F. H. Cameron personally, the Bank of Montreal, British Columbia, and the Toronto-Dominion Bank at Toronto and at Vancouver, "notwithstanding and the form or legal effect of the transactions".

Held also, that section 137(3) is no defence in this case as the applicability of s. 137(2) of the *Income Tax Act*, in that (1) this transaction was pursuant to and part of other transactions; (2) was not a *bona* *fide* transaction and (3) that, *inter alia,* one part of the series of transactions was not a transaction entered into by persons dealing at arm's length.

Appeals dismissed with costs.

INCOME TAX APPEALS.

Terence Sheard, Q.C. for appellants Conn Smythe and Clarence H. Day. *John G. Edison, Q.C.* for appellant Conn Stafford Smythe.

W. B. Williston, Q.C., A. D. Givens, G. W. Ainslie and *Peter F. Cumyn* for respondent.

GIBSON J.:—These three appeals are from the respective assessments for income tax made against the appellants contained in Notices of Re-Assessment dated 1966 for the taxation year 1961 and on consent were tried together on common evidence.

In each of the Notices of Re-Assessment and in the explanation of the changes from the prior assessments, the increase in taxes assessed and claimed was stated to be made on the premise that each of the appellants was deemed to have received a dividend arising out of what they received as a result of transactions in December 1961 concerning the shares held by each of them in the Ontario corporation known as C. Smythe Limited.

In December 1961, the common shares (which were the only shares) of C. Smythe Limited were owned and in the following proportions by:

Conn Smythe	52%
Conn Stafford Smythe	30.8%
Clarence H. Day	16%
and A. M. Boyd	1.2%

No proceedings have been taken by the respondent against A. M. Boyd in respect to this matter.

In December 1961 C. Smythe Limited had undistributed earned surplus of approximately $728,652 and capital gains which, when realized, might approximate $1,800,000.

The said shareholders of C. Smythe Limited before causing to be done any of the things that were done here, were aware of the incidence of income tax if any of this undistributed earned surplus or capital gains was paid to

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them or appropriated for their benefit by employing and complying with the provisions of either section 105[1] or 105B[2] of the *Income Tax Act*.

These appeals relate to what was done by a series of transactions in December 1961 in respect to the undistributed earned surplus of approximately $728,652 in C. Smythe Limited.

By these transactions, this said undistributed earned surplus was paid or appropriated to the shareholders of C. Smythe Limited, namely, the three appellants Conn Smythe, C. Stafford Smythe, Clarence H. Day, and A. M. Boyd (who was not a party to these proceedings). This payment or appropriation was in the form of $275,336 cash and $453,316 worth of non-interest-bearing debenture certificates in a newly incorporated company known as C. Smythe For Sand Limited.

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[1] 105. Corporation election.

(1) A corporation may elect, in prescribed manner and in prescribed form, to be assessed and to pay a tax of 15% on an amount equal to its undistributed income on hand at the end of the 1949 taxation year minus its tax-paid undistributed income as of that time.

(1a) In lieu of making any election under subsection (1), a corporation may, in any taxation year at a time when

(*a*) its undistributed income on hand at the end of the immediately preceding taxation year minus its tax-paid undistributed income as of the end of that immediately preceding taxation year.

is less than

(*b*) its undistributed income on hand at the end of the 1949 taxation year minus its tax-paid undistributed income as of the end of that taxation year,

elect, in prescribed manner and in prescribed form, to be assessed and to pay a tax of 15% on an amount equal to the amount determined under paragraph (*a*).

(2) A corporation other than a subsidiary controlled corporation

(*a*) whose undistributed income on hand at the end of its 1949 taxation year, if any, did not exceed its tax-paid undistributed income as of that time, or

(*b*) that has paid the tax payable by virtue of having made an election under subsection (1) or (1a),

may elect, in prescribed manner and in prescribed form, to be assessed and to pay a tax of 15% on an amount not exceeding

(*c*) the aggregate of

(i) the dividends declared by it that were paid by it in the taxation years beginning with the 1950 taxation year and ending with the last complete taxation year before the election under this subsection, and

In respect to this payment or appropriation, no income tax was paid by either C. Smythe Limited or by any of its said shareholders or A. M. Boyd personally.

There was no business reason for entering into these said transactions.

This series of transactions for all practical purposes began on November 17, 1961 when at a meeting of the directors of C. Smythe Limited authority was given to the President (Conn Smythe) to arrange for the distribution of $375,000 of this undistributed earned surplus of approximately $728,652 to the shareholders of C. Smythe Limited; and Mr. S. E. V. Smith of Price Waterhouse & Co., chartered accountants, Toronto Office, was employed to arrange for this to be done.

The said Mr. S. E. V. Smith acted as agent for the appellants (and A. M. Boyd) at all material times, and specifically in advising, negotiating and completing the preliminary transactions and the transaction between the appellants and two British Columbia companies by the names of F. H. Cameron Limited and Dabne Enterprises Limited, concerning the sale of the said shares held by each of them in C. Smythe Limited.

(ii) the dividends that were, by section 81, deemed to have been received by shareholders of the corporation in the taxation years referred to in subparagraph (i),

except such portions thereof as, by virtue of subsection (4) of section 81 or subsection (1) of section 141, have not been taken into account in computing income of shareholders of the corporation,

minus

(*d*) the aggregate of the amounts under which it has previously paid tax under this subsection or under subsection (2a) or (2b).

(2a) A subsidiary controlled corporation that is subsidiary to a personal corporation and

(*a*) whose undistributed income on hand at the end of its 1949 taxation year, if any, did not exceed its tax-paid undistributed income as of that time, or

(*b*) that has paid the tax payable by virtue of having made an election under subsection (1) or (1a),

may elect, in prescribed manner and in prescribed form, to be assessed and to pay a tax of 15% on an amount not exceeding

(*c*) the aggregate of

(i) the dividends declared by it that were paid by it in the taxation years beginning with the 1950 taxation year and ending with the last complete taxation year before the election under this subsection, and

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Certain steps had been taken earlier in 1961 to put the assets of C. Smythe Limited in more liquid form so that some form of corporate distribution could be made to its shareholders and this made possible the implementation of the said directors' decision of November 17, 1961 to distribute $375,000.

Up until about the middle of December 1961, a transaction invoking and pursuant to section 105B of the *Income Tax Act* with Greenshields Inc., Montreal Office, was being considered, but on December 20, 1961, the appellants finally decided to enter into the said transaction for the sale of their shares in C. Smythe Limited (which was eventually completed) with F. H. Cameron Limited and Dabne Enterprises Limited. Prior to that day, the appellants *qua* shareholders of C. Smythe Limited had caused it to enter into and complete other transactions, which enabled the appellants to make this decision and election on that day.

(ii) the dividends that were, by section 81, deemed to have been received by shareholders of the corporation in the taxation years referred to in subparagraph (i),

except such portions thereof as, by virtue of subsection (4) of section 81 or subsection (1) of section 141, have not been taken into account in computing income of shareholders of the corporation,

minus

(*d*) the aggregate of the amounts upon which it has previously paid tax under this subsection or under subsection (2) or (2b), and

(*e*) such part of the dividends described in subparagraphs (i) and (ii) of paragraph (c) as were paid by it, or were deemed to have been received by its shareholders, as the case may be, when it was a subsidiary controlled corporation and was not subsidiary to a personal corporation.

(2b) Other subsidiary controlled corporations. A subsidiary controlled corporation that is not subsidiary to a personal corporation and

(*a*) whose undistributed income on hand at the end of its 1949 taxation year, if any, did not exceed its tax-paid undistributed income as of that time, or

(*b*) that has paid the tax payable by virtue of having made an election under subsection (1) or (1a),

may elect, in prescribed manner and in prescribed form, to be assessed and to pay a tax of 15% on an amount not exceeding

(*c*) the amount determined under subsection (2) on which it would have been entitled to pay tax if, immediately before becoming a subsidiary controlled corporation, it had made an election under subsection (2) to pay tax thereunder,

minus

The relevant transactions which the appellants caused C. Smythe Limited to enter into and complete in December 1961 and the other transactions in 1962 were as follows:

In December 1961, the appellants caused a new Ontario corporation to be incorporated under the name of C. Smythe For Sand Limited of which they became the owners of the issued shares (which were common shares).

All assets of C. Smythe Limited were then transferred to C. Smythe For Sand Limited in exchange for a promissory note to the value thereof, *viz.*, $2,611,769.

On December 28, 1961, all the shares of C. Smythe Limited were sold to F. H. Cameron Limited and Dabne Enterprises Limited, two Vancouver-based corporations, incorporated under the British Columbia *Companies Act.* To accomplish this, certain transactions were entered into practically simultaneously: the appellants caused a temporary loan to be made to C. Smythe For Sand Limited

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(*d*) the aggregate of the amounts on which it has previously paid tax under this subsection.

(3) Payment of tax with election. An election under this Part is null and void unless, when the election was made, there was paid to the Receiver General of Canada

(*a*) if the election was made under subsection (1) or (1a), the amount of the tax as estimated by the corporation in the election, and

(*b*) if the election was made under subsection (2), (2a) or (2b), the amount of the tax that the corporation elected to pay.

(4) Deficient or excessive payments. Where an election was made under subsection (2), (2a) or (2b) and the amount of the tax paid with the election is in excess of or less than 15% of the amount on which, according to the election, the corporation elected to pay tax, the corporation shall be deemed to have elected to be assessed and to pay tax under that subsection on an amount equal to the lesser of

(*a*) 100/15 of the amount of the tax so paid, or

(*b*) the maximum amount on which it was entitled, at the time the election was made, to elect under subsection (2), (2a) or (2b), as the case may be, to be assessed and to pay tax.

(5) Where the estimated amount of tax under subsection (1) or (1a) that was paid with an election was in excess of or less than the amount payable under that subsection, tax shall be deemed to have been paid under this Part on an amount equal to the lesser of

(*a*) 100/15 of the estimated amount of tax so paid, or

(*b*) the amount on which the corporation was entitled, at the time the election was made, to elect under subsection (1) or (1a), as the case may be, to be assessed and to pay tax.

(6) Assessment. The Minister shall, with all due dispatch, examine each election made under this section, assess the tax payable and send a notice of assessment to the corporation.

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by the Toronto-Dominion Branch, Toronto, in order to pay off the said promissory note to C. Smythe Limited, thereby putting its assets in cash form; and F. H. Cameron Limited and Dabne Enterprises Limited obtained a temporary loan—"daylight loan" from the Bank of Montreal, Vancouver, B.C. to pay the appellants and A. M. Boyd for their shares in C. Smythe Limited; F. H. Cameron Limited and Dabne Enterprises Limited (*qua* new and then only shareholders of C. Smythe Limited) caused C. Smythe Limited to invest in preferred shares of F. H. Cameron Limited and Dabne Enterprises Limited equal to the amount (i.e., $2,611,769) of its cash assets, thereby putting cash in F. H. Cameron Limited and Dabne Enterprises Limited to enable them to pay off their "daylight" loan from the Bank of Montreal; and the appellants subscribed and paid for certain common shares and non-interest-bearing debentures of C. Smythe For Sand Lim-

(7) Payment of deficiency Where an election was made under subsection (1) or (1a), the corporation shall, within 30 days from the day of mailing of the notice of assessment, pay to the Receiver General of Canada an amount equal to the amount by which the tax payable exceeds the tax as estimated in the election, whether or not an objection to or an appeal from the assessment is outstanding, and shall, in addition, pay interest on that amount at 6% per annum from the day of the election until the day of payment whether or not it was paid within the period of 30 days.

(8) Time tax deemed to have been paid. Where the balance of the tax payable under subsection (1) or (1a) has been paid within 30 days of the day of mailing of the notice of assessment and interest, if any, payable under subsection (7) has also been paid within that time, the whole amount of the tax payable shall be deemed to have been paid under this Part on the day of the election.

(9) Application. Subsection (4) of section 46 and sections 58 to 61 are applicable *mutatis mutandis* to this Part.

[2] 105B Dividends paid out of designated surplus.

(1) Tax. Where a corporation other than a non-resident-owned investment corporation has in a taxation year paid a dividend the whole or any part of which would, if section 28 were applicable, be regarded as having been paid out of designated surplus of the corporation as determined under that section, and the corporation was, at the time the dividend was paid, controlled by

(*a*) a non-resident corporation,

(*b*) a person exempt from tax under section 62 other than a personal corporation, or

(*c*) a trader or dealer in securities,

the corporation shall, on or before the day on or before which it is required to file a return of income under Part I for the taxation year in which the dividend was paid, pay a tax equal to ited, with some of the money they received from this sale of their shares in C. Smythe Limited; and then both temporary loans were respectively repaid to the said banks by C. Smythe For Sand Limited and F. H. Cameron Limited and Dabne Enterprises Limited.

The net cash assets of C. Smythe Limited after this temporary bank loan was made, as stated, had a value of $2,611,769. The appellants and A. M. Boyd sold their shares for $2,570,336, or $41,433 less than the book value of these shares at the time.

The said sum of $41,433 was 5 per cent of $728,652 (the undistributed earned surplus of C. Smythe Limited) namely, $36,433, plus $5,000.

This $5,000 was added after Mr. S. E. V. Smith of Price Waterhouse & Co. had advised Mr. Conn Smythe that the exact computation at the time of the undistributed earned surplus of C. Smythe Limited was difficult, and Mr. Smythe had instructed that the shares of

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(*d*) 15%, in any case where paragraph (*a*) or (*b*) applies, or

(*e*) 20%, in any other case,

of the amount of the dividend or, as the case may be, the part thereof that would, if section 28 were applicable, be regarded as having been so paid.

(2) Determination of payment of dividend. For the purpose of determining whether or not a dividend or any part thereof would, if section 28 were applicable, be regarded as having been paid out of designated surplus of the corporation as determined under that section, if the corporation was controlled by a person described in paragraph (*b*) or (*c*) of subsection (1), such person shall, at all times relevant to that determination, be deemed to have been a corporation.

(3) Dividends deemed to have been paid. For the purposes of this section, dividends deemed by this Act to have been received from the payer corporation and that are required by this Act to be included in computing the recipient's income (or that would be so required if the recipient were resident in Canada at the time the dividends were so deemed to have been received) shall be deemed to have been paid by the payer corporation.

(4) Controlled corporation. For the purposes of this section, a corporation is controlled by a person described in paragraph (*a*), (*b*) or (*c*) of subsection (1) if more than 50% of its issued share capital (having full voting rights under all circumstances) belongs to that person, or to that person and to persons with whom that person does not deal at arm's length.

(5) For the purposes of subsection (4),

(*a*) issued share capital of a corporation belonging to or held by a trustee or one or more other persons beneficially for owners or members of an organization, club, society or other unincorporated association that is a person exempt from tax under section 62 shall be deemed to be issued share capital

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C. Smythe Limited were to be offered for sale to F. H. Cameron Limited and Dabne Enterprises Limited at a flat price not subject to any negotiation based on the exact computation at the time of sale of the amount of this undistributed earned surplus.

As a result of these transactions, the appellants and A. M. Boyd received the following amounts in cash and in non-interest-bearing debentures of C. Smythe For Sand Limited:

	Cash Paid	*Amount of non-interest-bearing debentures of C. Smythe For Sand Limited received*
Conn Smythe	$ 143,175	$ 1,193,400
Conn Stafford Smythe ..	84,763	706,900
Clarence H. Day	44,054	367,200
A. M. Boyd	3,344	27,500
TOTAL	$ 275,336	$ 2,295,000

In respect to the said sum of $275,336 in cash received by them and $453,316 of the total of non-interest-bearing-debenture certificates, which amounts together equal

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of the corporation belonging to the organization, club, society or other association, as the case may be, as a person so exempt; and

(*b*) members of a partnership shall be deemed not to deal with each other at arm's length.

(6) Exception where shares acquired by gift or bequest. No tax is payable under subsection (1) where the payer corporation was, at the time a particular dividend was paid by it, controlled by a person exempt from tax under section 62, if all of the issued share capital of the corporation (having full voting rights under all circumstances) that, during the period defined in subsection (4) of section 28 as the "control period", belonged to that person or to that person and persons with whom that person did not deal at arm's length, was acquired by that person (or by that person and persons with whom that person did not deal at arm's length) by way of unconditional gift or unconditional bequest.

(7) Interest. Where a corporation is liable to pay tax under subsection (1) and has failed to pay all or any part thereof on or before the day on or before which it was required to pay the tax, it shall, on payment of the amount in default, pay interest at 6% per annum from the day on or before which it was required to make the payment to the day of payment.

(8) Return. Every corporation that is liable to pay tax under subsection (1) shall, on or before a day on or before which it is required to pay the tax, file a return of information in prescribed form relevant to the transaction or transactions giving rise to such tax.

(9) Section 46 and sections 55 to 61 are applicable *mutatis mutandis* to this Part.

$728,652, the amount of the said undistributed earned surplus of C. Smythe Limited, the appellants and A. M. Boyd as stated did not consider any part of the same as income within the meaning of the *Income Tax Act*, and accordingly did not declare their respective shares of these monies and debentures received as income in their individual tax returns for 1961, and in consequence, no income tax was paid by any of them in respect of the receipt of these monies and debentures.

In respect to these said receipts of cash and non-interest-bearing debentures in C. Smythe For Sand Limited, each of the appellants in May 1966 received Notices of Re-Assessment, increasing their respective income tax for the year 1961, and demanding such increase in tax as follows, (exclusive of interest also demanded):

Mr. Conn Smythe	$203,205.18
Mr. C. Stafford Smythe	$110,581.65
Mr. C. H. Day	$ 41,714.70

Counsel for the appellants have made the following calculation of the income tax assessed by each of these reassessments as follows:

CONN SMYTHE
CALCULATION OF INCOME TAX ASSESSED
ON MAY 25, 1966 IN RESPECT OF 1961

Revised taxable income per re-assessment		$468,227.82
	Taxable Income	
Tax per form	$400,000.00	$269,160.00
	68,227.82	54,582 26
	$468,227.82	323,742.26
Less:		
Dividend tax credit—20% of $424,574.79		84,914.95
Dividends—per return	$ 45,675.75	
per re-assessment	378,899.04	
	$424,574.79	
Tax per re-assessment notice		$238,827.30
Undistributed income on hand of C. Smythe Limited at December 28, 1961 per balance sheet at that date and detailed schedules		$728,652.00
52% (Conn Smythe share)		$378,899.04

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C. STAFFORD SMYTHE
CALCULATION OF INCOME TAX ASSESSED
ON MAY 30, 1966 in respect of 1961

Taxable income declared and as re-assessed 1962	$ 37,355 61	
Added by Re-Assessment 1966	233,168 64	
Revised taxable income per re-assessment	$270,524 25	
	Taxable Income	
Tax (at 1961 rates)		
on first	$225,000.00=	$137,910 00
on balance of	45,524 25=	34,143 19
	$270,524.25	$172,053 19
Less:		
Dividend tax credit—20% of $244,773 39		48,954 68
Dividends—per Return	$ 11,604.75	
—per re-assessment	233,168 64	
	$244,773 39	
		$123,098 51
Less.		
Foreign tax credit per Return		14.26
Tax per Re-Assessment Notice		$123,084.25
Undistributed income on hand of C Smythe Limited at December 28, 1961 per balance sheet at that date and detailed schedules		$728,652 00
32% (C Stafford Smythe share)		$233,168 64

CLARENCE H. DAY
CALCULATION OF INCOME TAX ASSESSED
ON JUNE 1, 1966 in respect of 1961

Taxable income declared	$ 25,862 65	
Added by Re-Assessment	116,584.32	
Revised taxable income per re-assessment	$142,446 97	
	Taxable Income	
Tax per form	$125,000 00	$ 67,910 00
	17,446 97	12,212 88
	$142,446.97	$ 80,122.88

Less.		
Dividend tax credit—20% of $125,339.92		25,067 98
Dividends—per Return	$ 8,755 60	
per re-assessment	116,584 32	
	125,339 92	
		55,054.90
Less.		
Foreign tax credit per Return		11 24
Tax per Re-Assessment Notice		55,043 66
Undistributed income on hand of C. Smythe Limited at December 28, 1961 per balance sheet at that date and detailed schedules		$728,652 00
16% (Clarence H Day share)		$116,584.32

One preliminary matter was argued by counsel, that is to say: counsel for the appellants submitted (and the Notices of Re-Assessment and the explanatory data accompanying the same on Department of National Revenue form T7W-C indicate) that the assessments were made on the basis of a deemed receipt of a dividend pursuant to section 81(1)[3] of the *Income Tax Act*; and that the respondent is not entitled as he did in his pleadings by way of reply to allege further facts and to plead other sections of the *Income Tax Act* to support these re-assessments.

Counsel for the respondent on the other hand, submitted that the respondent is not bound by the assumptions made by the assessor or the statement of reasons given in the Notice of Assessment or Re-Assessment for the assessment or re-assessment or by the section or sections of the *Income Tax Act* referred to, purporting to establish the basis for the assessment for tax, but is entitled to allege further facts and rely on other sections of the *Income Tax Act* in his

[3] 81. Undistributed income on hand.

(1) Where funds or property of a corporation have, at a time when the corporation had undistributed income on hand, been distributed or otherwise appropriated in any manner whatsoever to or for the benefit of one or more of its shareholders on the winding-up, discontinuance or reorganization of its business, a dividend shall be deemed to have been received at that time by each shareholder equal to the lesser of

(*a*) the amount or value of the funds or property so distributed or appropriated to him, or

(*b*) his portion of the undistributed income then on hand.

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pleadings in proceedings in this Court contesting such assessment or re-assessment, but that in the case of the latter course of action by the respondent that the onus is on the respondent to prove the same; and that in exercise of this right further facts were alleged and other sections of the *Income Tax Act* were pleaded to support these re-assessments.

I am of opinion that the respondent is not bound by the assumptions made by the assessor or the reasons stated in the Notices of Assessment or Re-Assessment and is not restricted to relying on the reasons stated or the section or sections of the *Income Tax Act* referred to, purporting to be the basis for the assessment or re-assessment for income tax, but is entitled to allege in his pleadings in this Court other facts and to plead any other alternative or additional section or sections of the *Income Tax Act* as the basis for asking this Court to confirm or otherwise adjudicate upon any assessment or re-assessment for income tax; but in so far as the latter procedure is adopted by the respondent, the onus of proof is on him. (See *Roderick W. S. Johnston v. M.N.R.*[4]; *The Minister of National Revenue v. Pillsbury Holdings Limited*[5]; and *British Columbia Power Corporation Limited v. M.N.R.*[6]).

So much for the preliminary objection.

As to the main issues for decision in these cases, a more detailed statement of the facts is now given.

Prior to November 1959, the shareholders of C. Smythe Limited were aware of the incidence of income tax in respect to undistributed surplus income of the company if distributed, and of the then existing provisions of the *Income Tax Act* whereby special sections had been enacted to lighten the burden of so-called "double taxation" of income from a corporation upon which income tax had been paid at corporation rates, coming into the hands of an individual shareholder. They knew that certain statutory conditions had to be complied with before advantage could be taken of such provisions of the Act. I refer to section 95A of the 1948 *Income Tax Act* (now section 105 of the present *Income Tax Act*). On more than one occasion prior to that time, the shareholders of C. Smythe Limited availed

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[4] [1948] S.C.R. 486 at 489.
[5] [1965] 1 Ex C.R. 676 at 686.
[6] 66 D.T.C. 5310 at 5311.

themselves of this statutory relief to obtain part of the undistributed surplus income of that company (see Exhibits R-63 and R-64).

Between November 3, 1959 and November 16, 1961 the shareholders of C. Smythe Limited were also advised by Mr. S. E. V. Smith of Price Waterhouse & Co. of various plans and arrangements whereby they might be paid the undistributed earned surplus and the capital gains of that company.

For example, by letter of November 3, 1959 (see Exhibit R-4), Mr. Smith wrote to Mr. Conn Smythe, the President of C. Smythe Limited, explaining to him the tax implications of invoking respectively the provisions of sections 105 and 105B of the *Income Tax Act,* and specifically in respect to the latter outlining a plan or arrangement in which the approximate cost for taxes and other charges Mr. Smith estimated to be $150,000. That letter reads as follows:

PRICE WATERHOUSE & CO.

55 Yonge Street
TORONTO 1
November 3, 1959.

CONFIDENTIAL

Conn Smythe, Esq., President,
C Smythe, Limited,
Postal Station "D", Box 8,
Toronto.

Dear Mr. Smythe:

With reference to your recent letter we have considered various methods whereby the shareholders of your company might be paid the balances of earned surplus and capital gain arising from sale of fully depleted gravel properties which together amounted to $1,326,508 at February 28, 1959.

Section 95A of the 1948 Income Tax Act is now Section 105 of the present Income Tax Act. This section is not too useful in your case where it is desired to distribute to shareholders a substantial amount of undistributed income and capital gains. This is so because to get out the capital gains tax free it is necessary to first dispose of all of the undistributed income. In order to do this under Section 105 it would be necessary to pay out 50% of earned surplus (viz. about $350,000) in cash dividends in, say, 1959 in order to make an election on an equal amount in 1960 on which tax of 15% would be paid This would give rise to very substantial personal income tax on the cash dividends in one year; if the procedure were spread out over a number of years it has the disadvantage that subsequent earnings also have to be paid out to the extent of 50%. This latter difficulty could be overcome by forming a new operating company and thus avoid annual increases in earned surplus of C. Smythe,

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Limited but we believe that, in view of the high personal rates of tax payable by you and your fellow shareholders, the alternative plan set out below might be more attractive

In outlining this plan we are assuming for simplicity that the amounts of earned surplus and capital gains from sale of depleted properties at the time you contemplate any action are the same as those carried on the company's books at February 28, 1959 You will also observe that under the plan a substantial tax payment is required and thus there would be no point in carrying it out unless fairly substantial sums of cash were made available from the sale to outsiders of marketable securities or Jane Street properties.

Since the proposal set out hereunder involves the interpretation of income tax legislation it should be reviewed by the company's solicitors. It might also be desirable to clear it in advance with income tax authorities but this is a matter which we could discuss later.

Section 105B, which is a fairly recent addition to the Income Act, contains provisions whereby:

(*a*) a non-resident corporation holding all of the stock of a Canadian company could get out the undistributed income by payment of a tax of 15% plus an additional withholding tax of 5%, except possibly in the case of distribution to a corporation resident in the United Kingdom which owned all the outstanding shares of the company, or

(*b*) a dealer in securities owning all of the stock of a Canadian company could get out the undistributed income by payment of a tax of 20%.

In a liquidation of the Canadian company the effective rate of these taxes would be somewhat reduced because the tax under Section 105B would be allowed as a deduction in computing the undistributed income subject to tax Accordingly it is possible that a non-resident corporation or a dealer in securities might be willing to purchase the shares of C. Smythe, Limited for an amount equal to the net assets of the company, less the estimated tax, and a profit for the work and risks involved in liquidating the company. The profit in such a transaction might run to from $10,000 to $35,000, depending on the time required, the risks involved and how good an arrangement you could negotiate. Thus in the case of your company the entire capital stock, premium on shares, capital gain from sale of depleted gravel properties and earned surplus might be made available tax free to the shareholders of C Smythe, Limited at an overall cost for taxes and other charges of about $150,000. The mechanics of carrying out the plan would be as follows:

1. A new operating company, say, Smythe Sand & Gravel Limited, would be incorporated by the shareholders of C. Smythe, Limited with the same percentage interest in the new company. Smythe Sand & Gravel Limited, would buy at book value all the assets of C. Smythe, Limited except the remaining Jane Street properties and marketable securities and would carry on the sand and gravel operations at Caledon.

2. The remaining Jane Street properties would be sold to Roseland Homes Limited at appraised values. This would give rise to a further capital gain from sale of depleted properties on the books of C. Smythe, Limited and any profit or loss on ultimate disposal of the properties would enter into the income tax

calculation of Roseland Homes Limited. (The appraised value should be as close as possible to estimated realizable value in order to avoid any undue taxable profit or loss in the hands of Roseland)

3. C Smythe, Limited would sell a portion of its marketable securities to outsiders for cash Any remaining marketable securities would be sold to the present shareholders of C. Smythe, Limited in the same ratio as their shareholdings, or to the new operating company, at fair market value on the date of sale. The sale of the securities would give rise to a capital profit which should not be subject to tax in the hands of C. Smythe, Limited or in the hands of its shareholders.

4. In the first instance the sale of assets to the new operating company and to Roseland Homes Limited would be carried on open account but immediately before the transaction referred to in 5 below the companies would obtain short term loans and pay off their indebtedness in cash. After all assets of C. Smythe, Limited have been sold to the new operating company, Roseland Homes Limited and outsiders, the new operating company would assume the liabilities of C. Smythe, Limited. The latter company would then be left with cash equal to the sum of the capital stock accounts, premium on shares, capital gains and earned surplus

5 At that stage the shareholders of C. Smythe, Limited would sell their shares of that company to a United Kingdom non-resident corporation or to a dealer in securities at an amount equal to the cash on hand less about $150,000 to cover income taxes payable and a profit for the buying corporation The net proceeds from the sale would be paid to the shareholders in cash by the purchaser who could then proceed to liquidate C. Smythe, Limited.

6. The cash received by the shareholders would be advanced to the new operating company and Roseland Homes Limited to the extent necessary to liquidate their short term borrowings and the balance of the proceeds would be held tax free by the shareholders. Presumably the advances would be evidenced by debentures or notes issued by Roseland Homes and the new operating company. As funds became available from the ultimate disposal of the remaining Jane Street properties held by Roseland Homes and from operations of the new operating company, the debentures or notes would be paid off and the cash would flow to the former shareholders of C. Smythe, Limited tax free

On the basis of current estimates which would be subject to revision in the light of conditions prevailing at the time the foregoing plan was carried out, we are setting out an example of how the proposed arrangement might work out:

Net book value of C Smythe Limited at February 28, 1959	$1,382,508
Excess of selling price of investments in common stocks of Canadian corporations over cost (Note 1), say	600,000
Proceeds from sale of fully depleted sand and gravel properties at Jane Street, say	375,000
Net book value of C Smythe Limited at date of sale	$2,357,508

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Less—Difference between net book value and amount received from the purchaser of shares of C. Smythe, Limited, say	150,000
Cash proceeds received by present shareholders of C. Smythe, Limited on sale of their shares (not subject to income tax)	$2,207,508
Less—Amount required to be advanced to the new operating company and to Roseland Homes Limited (Notes 1 and 2)	1,385,341
Net tax free proceeds available forthwith to the shareholders of C Smythe, Limited	$ 822,167

Notes:

1 It has been assumed that $750,000 has been received from outsiders for a portion of the investment in common shares and that the remainder have been sold to the shareholders of C. Smythe, Limited or to the new operating company at fair market value.

2 The amounts advanced to the new operating company and Roseland Homes Limited would be received free of tax when those companies pay off the advances to the present shareholders of C. Smythe, Limited.

We realize that the foregoing plan sounds complicated but in practice we believe that it could be carried out fairly simply, is within the framework of the Income Tax Act, and should enable a full release of the present net book value of C. Smythe, Limited. There are several further factors to be considered if any such arrangement were consummated but they are largely of a technical nature and we have not set them out herein We might mention, however, that the final sale of shares of C. Smythe, Limited would be carried out over a period of a day or two so that there should be little or no interest payable on the short term borrowings.

We feel that a discussion of the various factors involved would be helpful before any action is taken and when you have had an opportunity of reviewing this letter we shall be pleased to discuss it with you and your solicitors.

In case you may wish to pass this letter on to the other shareholders of the company we are enclosing additional copies.

Yours very truly,
(S. E. V. Smith)

Aside from the desire of shareholders of C. Smythe Limited to obtain cash for themselves from some or all of the undistributed earned surplus and capital gains of C. Smythe Limited, was the desire by the appellant Conn Smythe to implement an estate plan for himself. The reason for this was that approximately 50 per cent of his personal assets were represented by his shareholdings in C. Smythe Limited, and at that time, the liquid assets of C. Smythe Limited were relatively small in relation to the said total of undistributed earned surplus and capital gains. As a consequence, as was pointed out to Mr. Conn Smythe by his personal solicitor, Mr. I. S. Johnston, Q.C., if he should at that time die, the incidence of income tax and estate tax would be most substantial if nothing were done in relation to C. Smythe Limited, whereas, if a proper and legal estate plan was implemented, the burden of these taxes would be lessened.

(As mentioned, the first thing that was done in fact was to sell off certain of the non-liquid assets of C. Smythe Limited, namely, the depleted gravel pits and the shares owned by it in Maple Leaf Gardens Limited and thereby there was put substantial amounts of cash in the hands of C. Smythe Limited to enable a corporate distribution to be made. But these appeals have nothing to do with the actions in putting the assets of C. Smythe Limited in such liquid form in 1961.

What these appeals have to do with, is in relation to what was done after that and specifically in December 1961 in connection with the undistributed earned surplus of $728,652 of C. Smythe Limited.)

Again on June 28, 1961, Mr. S. E. V. Smith sent a further proposal to Mr. Conn Smythe. This letter reads as follows and the proposal enclosed with it is also set out:

Copy for Mr. Ian S Johnston, Q.C.
PRICE WATERHOUSE & CO.

55 Yonge Street
TORONTO 1
June 28, 1961.

Personal

Conn Smythe, Esq.,
Maple Leaf Gardens Limited,
Church and Carlton Streets,
Toronto.

Dear Mr. Smythe:

As arranged, I am handing you three copies of a preliminary draft of a memorandum concerning a possible rearrangement of the affairs of C. Smythe, Limited and its associated companies, Roseland Homes Limited and Conn Smythe Contracting Company Limited.

There are two or three factors bearing on the rearrangement which are not included in the memorandum and which I would prefer to discuss with you at the meeting on Thursday morning. One of them might well be discussed with Mr. G. R. Gardiner.

I am also enclosing copy of a memorandum concerning the possible formation of a personal corporation to facilitate your own estate planning.

Yours sincerely,
S. E. V. Smith

Enc-Draft memorandum (3)

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Memorandum
c c to Mr. Ian S Johnston.

Memorandum for Mr. Conn Smythe.

PERSONAL ESTATE PLANNING

The income and estate tax problems concerning your horse racing and breeding stable operations and the desirability of reorganizing the corporate structure of C Smythe, Limited, Conn Smythe Contracting Company Limited and Roseland Homes Limited are both the subject of separate memoranda. The sole purpose of this memorandum is to recommend a course of action which we believe will simplify the ultimate administration of your affairs by your executors.

We recommend that you form a personal corporation, say, Conn Smythe Limited, under the Ontario Companies Act, which would hold your principal bank accounts, all of your stocks and bonds, all of your real estate and any life insurance payable to your estate; your horses would not be included in the holdings of the corporation. This company would have a nominal share capital of, say, 1,000 shares issued at $1 00 each, of which you would hold, say, 997 and your three executors would hold the remaining three shares. The balance of the consideration for the purchase of your various assets by the personal corporation would be carried in an open account payable to you; this is the most flexible method.

The by-laws of the company could place whatever restrictions you might wish on the transfer or use of any assets For example, there might be a complete restriction on the sale of Maple Leaf Gardens shares except for the benefit of your heirs, and a provision that they be included in a voting trust subject to voting by you or, in your inability to act, by your son, Stafford Smythe, or, failing his ability to act, by your nominee

There are no income or estate tax advantages in such a corporation since income on assets owned by the corporation has to be taken up in your personal income tax return annually. The advantage which we believe is sufficiently important to justify the incorporation expenses involved is that during any incapacity by you, or in the event of your death, the other directors could deal promptly with the assets. This is particularly important after death since transfer of assets is dependent on obtaining releases from the federal estates tax department and the Ontario succession duty department. Such releases might be held up for a year or more until all estate matters are settled and certainly there is considerable inconvenience and difficulty in obtaining releases for the sale of real properties and securities. In the meantime severe losses might be suffered in a time of falling market values Through a personal corporation only the shares of the personal corporation would be subject to restrictions on transfer and the other directors of the company, who would be your executors, would be able to deal promptly with any assets of the estate.

PRICE WATERHOUSE & CO
(S E. V. Smith)

TORONTO, June 26, 1961.

Preliminary draft for discussion purposes only

Memorandum for the Shareholders of C. Smythe, Limited.

This memorandum has been prepared for the shareholders of C. Smythe, Limited in order to outline a desirable method of reorganization which would also take into account Roseland Homes Limited and Conn Smythe Contracting Company Limited. (The latter companies are relatively unimportant as compared with C. Smythe, Limited) The necessity for such a reorganization, the benefits to be obtained, and the broad plan are set forth herein. Particulars of certain steps involved are set forth in Appendix B attached.

The basic problem of the three main shareholders of C. Smythe, Limited, and in particular of Conn Smythe and C. H. Day, is that a substantial portion of their personal estate is tied up in C. Smythe, Limited. If any of the shareholders died, the valuation of C. Smythe, Limited would be based on the value of the company without taking into account any income taxes payable on a total or partial distribution of assets necessary to provide for succession duties and the beneficiaries of the estate. Furthermore, the company has accumulated substantial capital gains from the sale of fully depleted gravel properties at Jane Street and from the sale of marketable securities, which cannot be put into the hands of the shareholders except by the payment of substantial dividends to individuals or until tax has been paid on the accumulated earned surplus, which amounted to $644,003 at February 28, 1961.

In this memorandum we are using amounts shown in the audited accounts of the companies as of February 28, 1961. When a reorganization is carried out, the accounts of the companies should be brought up to date. Although it would not be necessary to audit them, they should be reviewed by Price Waterhouse & Co. in order that all normal accruals and adjustments usually made only at fiscal year-ends are taken into account.

In our opinion it is most desirable to reorganize the companies in such a way that the assets of the shareholders may be more readily realized upon. If is also important that income taxes and other costs payable on distribution of accumulated earnings, which would probably aggregate a minimum of $150,000, be paid <u>now</u> in order that estate asset values of the shareholders may be reduced accordingly.

We have considered various methods by which a reorganization might be carried out and, to the best of our ability, have taken into account the various interests of the three main shareholders. It should be recognized that modifications may be necessary if further information is brought out as a result of discussions between the shareholders and us.

In our opinion, the plan set forth herein should be the most economical from the standpoint of income taxes, legal and accounting fees and, as far as we know, falls within the framework of present income tax legislation. It should not be carried out until the final 1961 federal budget legislation is adopted since technical amendments to the Income Tax Act are sometimes introduced at a late date, but it should be carried out as soon as possible after that time.

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The proposed plan of reorganization is set out hereunder:

1. The four shareholders of C. Smythe, Limited would cause the shareholdings of Roseland Homes Limited and Conn Smythe Contracting Company Limited to be rearranged in such a way that the shares of all three companies would be owned in the following ratios:

Conn Smythe	52%
C. S. Smythe	30 8%
C. H. Day	16%
A M. Boyd	1.2%

(Details of the steps required are set out in Appendix B(1))

2. C. Smythe, Limited, Roseland Homes Limited and Conn Smythe Contracting Company Limited would merge under the amalgamation provisions of Section 96 of the Ontario Corporations Act into a new company, say, C. Smythe (1961) Limited.

3. C. Smythe (1961) Limited would sell all of its operating assets, including cattle and Caledon sand and gravel properties, to a new operating company, Smythe Sand & Gravel Limited The assets would be sold at fair market value except for Caledon sand and gravel properties and other depreciable assets which would be sold at values established for tax purposes. The new company would pay for the assets purchased by the issue of 10,000 common shares at 10¢ each ($1,000) and 5% income debentures for the balance ($683,296). The new operating company would provide for working capital through bank loans or loans from shareholders. (A pro forma balance sheet setting out the position of the new company is attached as Appendix A.)

4. The shareholders of C. Smythe (1961) Limited would purchase their share of all remaining assets of the company (viz. investments in bonds and stocks, mortgage due on Jane Street property, the remaining Jane Street property, and the common shares and 5% income debentures of Smythe Sand & Gravel Limited) at fair market value. It may appear that the use of market values for the investments, particularly the shares of Maple Leaf Gardens Limited might be undesirable, but it has no real effect on the shareholders of C. Smythe, Limited since they are simply transferring their portion of the assets held by the company to their personal possession.

   As a practical matter the mortgage on the Jane Street property and the remaining Jane Street property should probably be sold to a liquidating trust which would collect interest and payments on capital from the mortgage and sale of land and distribute them to the shareholders as collected.

   Also, it is contemplated that all shares of Maple Leaf Gardens Limited would be put under the control of a voting trust whereby dividends therefrom would flow directly to the individual shareholders concerned but voting of the shares would be done by Conn Smythe, or failing him, C. S. Smythe, or failing them, their nominee.

5. The shareholders would pay cash for the assets referred to in Item 4 above. Immediately thereafter they would sell all of

their shares in C. Smythe (1961) Limited to a non-resident United Kingdom corporation for cash at a price which would be equivalent to the shareholders' equity in C. Smythe (1961) Limited, after taking into account capital gains on all dispositions of Jane Street property and investments in common stocks, less income taxes and other costs arising from reorganization and effective distribution of the assets of C. Smythe, Limited, Roseland Homes Limited and Conn Smythe Contracting Company Limited. (This transaction could be carried out through a dealer in securities but the tax on undistributed income would be 5% higher.)

The net results of the foregoing plan may be summarized as follows (values at February 28, 1961 are used in all cases and the sale price of the remaining Jane Street property has been taken to be $250,000):

Net book value of C. Smythe, Limited	$1,590,244	
Add:		
Excess of market value of investments in common stocks of Canadian corporations over cost	432,820	
Market value of remaining fully depleted sand and gravel property at Jane Street	250,000	
Adjusted net book value of C. Smythe, Limited		$ 2,273,064
Net book value of Roseland Homes Limited	$ 23,880	
Add—Excess of market value of investments in marketable securities over cost	10,866	
Adjusted net book value of Roseland Homes Limited		34,746
Net book value of Conn Smythe Contracting Company Limited		27,114
Adjusted net book value of the merged corporation, C. Smythe (1961) Limited		$ 2,334,924
Less—Cost of income taxes payable on undistributed income of merged corporation and other items, (estimated $125,000 to $150,000) say		150,000
		$ 2,184,924
Less—Amount invested in the new operating company, Smythe Sand & Gravel Limited (See pro forma balance sheet—Appendix A)		684,296
Balance of assets available for pro rata distribution *tax free* to shareholders		$ 1,500,628

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These assets would comprise:

Cash			$ 25,134
Government of Canada bonds			100,800
Marketable securities at market value—			
	Shares	*Market value*	
Maple Leaf Gardens Limited	29,728	$ 836,100	
Milton Brick Co. Ltd.	34,865	78,446	
The Jockey Club Limited	10,000	29,000	
Canadian Collieries Resources Limited—			
Common	3,275	20,878	
5% Preferred	10,000	7,600	
The International Nickel Company of Canada, Limited	260	16,900	
Noranda Mines Limited	100	4,200	
Standard Paving & Materials Ltd.	100	1,650	
			994,774
Mortgage receivable on Jane Street property			129,920
Jane Street property, at market value			250,000
			$ 1,500,628

The basic benefits of the foregoing rearrangement for the shareholders of C. Smythe, Limited may be summarized as follows:

1. Cash, marketable securities and other assets resulting from capital gains in C. Smythe, Limited and Roseland Homes Limited are put into the hands of the individual shareholders at a minimum income tax cost.

2. The combined potential estate value of the shareholders is reduced by $150,000.

3. Through holding separate marketable securities, etc. the shareholders can carry out their own estate planning on a more flexible basis.

4. The income debentures of the new company, Smythe Sand & Gravel Limited, owned by a shareholder, could, in the event of his death and by an agreement between the shareholders, be paid to his estate through raising a mortgage on Caledon sand and gravel properties or by other means.

5. If desired, the shareholders' interests could be rearranged. For example, C. H. Day could sell his common shares in the new operating company, Smythe Sand & Gravel Limited, to C. S. Smythe at fair market value and take 5% income debentures owned by Smythe in payment thereof.

Similarly Conn Smythe could sell all or most of his interest in the new company to C. S. Smythe and take income debentures of the new company and other obligations of C. S. Smythe. Under this method Conn Smythe could still retain voting control through having a majority of the common shares of Smythe Sand & Gravel Limited, subject to an irrevocable proxy to be voted by him during his lifetime. A benefit from this course would be to establish estate values for Conn Smythe's interest in the Caledon properties now and to freeze them at this figure with any growth going to C. S. Smythe.

Alternatively, arrangements could be worked out so that the beneficiaries of Conn Smythe's will might hold his common shares in Smythe Sand & Gravel Limited subject to Conn Smythe's voting control during his lifetime.

All such alternatives and details could only be dealt with in the light of the wishes of the interested parties and after thorough and complete discussion and consideration.

The important step now is to carry out the basic essentials of the plan which is to pay income tax on the undistributed income of the various companies so as to reduce the individual shareholders' inheritance tax, to get assets in their hands which may be more readily liquidated, and put their personal affairs in a more flexible condition if any one of them should die.

PRICE WATERHOUSE & CO.
(S. E. V. Smith)

TORONTO, June 26, 1961.

Appendix A

SMYTHE SAND & GRAVEL LIMITED
(a new company)

PRO FORMA BALANCE SHEET AS AT FEBRUARY 28, 1961

After giving effect to the following transactions:

1. The purchase of all Caledon sand and gravel operating assets, including cattle and trucks, by Smythe Sand & Gravel Limited, a new company.
2. The settlement of the purchase price by—
   (a) the issue of 10,000 common shares for 10¢ each
   (b) the issue of 5% income debentures in the amount of $683,296.

ASSETS

Current Assets:			
Trade accounts receivable less allowance for doubtful accounts of $10,000			$ 123,965
Other receivables			3,243
Inventory of feeder cattle, at cost			62,670
			$ 189,878
Fixed Assets, at cost:			
Sand and gravel properties, including buildings	$ 622,267		
Less—Accumulated depletion and depreciation	206,461		
		$ 415,806	
Plants and equipment	$ 959,318		
Furniture and fixtures	20,574		
Trucks and automobiles	105,136		
	$ 1,085,028		
Less—Accumulated depreciation	861,930		
		223,098	
			638,904
			$ 828,782

LIABILITIES

Current Liabilities:	
Accounts payable and accrued liabilities	$ 66,486
Mortgage payments due within one year	24,000
	$ 90,486
Mortgages Payable (exclusive of amounts due within one year)	54,000
5% Income Debentures	683,296
	$ 827,782
Capital Stock Issued:	
10,000 no par value common shares for 10¢ each	1,000
	$ 828,782

Appendix B

1. In order to carry out a satisfactory merger of C. Smythe, Limited, Roseland Homes Limited and Conn Smythe Contracting Company Limited it is necessary that the shareholdings of Conn Smythe, C. S. Smythe, C. H. Day and Arthur M. Boyd be in the same ratio for the three corporations. (Any outstanding preference shares of C. Smythe, Limited should be redeemed before the merger.) The ratio of present shareholdings in C. Smythe, Limited is as follows:

Conn Smythe	52%
C. S. Smythe	30.8%
C. H. Day	16%
A. M. Boyd	1.2%

To bring the common share ownership of the other companies into the same relationship the following transactions would need to be carried out:

(a) Roseland Homes Limited—
I. E. Smythe should sell 100 shares to C. S. Smythe.
M. Holt should sell 100 shares to C. S. Smythe.
H. Smythe should sell 100 shares to C. S. Smythe.
C. H. Day should sell 70 shares to C. S. Smythe and 30 shares to A. M. Boyd.

(b) Conn Smythe Contracting Company Limited—
Conn Smythe should sell 40 shares to C. S. Smythe.
C. H. Day should sell 6 shares to Arthur M. Boyd and 14 shares to C. S. Smythe.

For practical purposes the sale price of these shares could be fixed at their book value adjusted upwards in the case of Roseland Homes for the excess of market value of common stocks over cost and, in each case, reduced by 20% of undistributed income on hand. On this basis the value per share of Roseland Homes Limited and Conn Smythe Contracting Company Limited at February 28, 1961 would be $12.01* and $43.53 respectively.

*This price is price as based on capital stock issued for a consideration of $1 00 of which only 10 cents has been paid up. Before any merger it would probably be advisable to have the additional 90 cents per share paid up on the stock of Roseland Homes Limited. Such payments would be recovered by the shareholders on liquidation.

2. The merger of the corporations would present no particular problems, except to carry out the necessary legal requirements, and the shareholders of the merged corporation would have the same percentage ownership as they now have in C. Smythe, Limited.

3. The merged corporation would sell all of its operating assets, including Caledon sand and gravel properties, cattle and trucks now owned by Conn Smythe Contracting Company Limited to the new operating company, Smythe Sand & Gravel Limited. Except for depreciable assets and cattle, we would expect that fair market value would be equivalent to book value. In the case of cattle, which are carried at cost on the books, fair market value would likely be somewhat higher; such values based on the best estimates of company officials should be used. Depreciable assets should be transferred,

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including Caledon sand and gravel properties, to the new operating company at tax values in order that there may be no recapture of depreciation for tax purposes.

The new operating company should be able to take the same depreciation rate, viz. 6¢ per ton, now allowed to C. Smythe, Limited. Obviously, we cannot guarantee that this would be accepted by income tax authorities but, in speaking to a senior member of the Toronto District Office, he indicated that there was no reason, in a non-arm's length transaction such as this, why the Department would require a new engineering estimate of the property. He stated that the rate had been determined once in accordance with the Department's regulations and that, in his opinion, the rate of 6¢ could be used by the new company. Although no names were mentioned, it is probable that he had C. Smythe, Limited in mind.

4. In selling the assets of the merged corporation, C. Smythe (1961) Limited, to its shareholders, fair market value should be used. For this purpose quoted market prices would be used for marketable securities, book value for mortgages, and an appraised value for the Jane Street property. It would be preferable if the Jane Street property were sold and the mortgage or other proceeds were available for distribution to the shareholders, but there is some chance that if it were sold to a trust for liquidation, any subsequent excess over the transfer price could be treated as a capital gain for tax purposes.

Under this proposal of Mr. Smith, as noted, the estimated income tax cost if it had been implemented would have been between $125,000 and $150,000; and under it, a new operating company would have been incorporated which would buy and pay for the assets of C. Smythe Limited by issuing 10,000 common shares at 10c per share and 5 per cent income debentures for the balance of the purchase price.

Then on July 5, 1961, at a meeting of the shareholders of C. Smythe Limited at which Mr. C. H. Day was not present, Mr. Smith advised that there were "two methods talked about in current tax literature whereby undistributed earnings of a company could be distributed tax free" and that he "was very reluctant to recommend such methods since he felt that they might be successfully attacked by income tax authorities".

As a result of that meeting, Mr. Conn Smythe expressed the opinion that the *status quo* of C. Smythe Limited was satisfactory and Mr. C. Stafford Smythe expressed the opinion that the cost of $150,000 for income tax and other items was too great for the benefits to be achieved.

On the same day July 5, 1961, Mr. Smith wrote Mr. C. H. Day informing him of these proposals and of these opinions expressed by Messrs. Conn Smythe and C. Stafford Smythe (see Exhibit A-3) and that letter reads as follows:

Copy for Mr. Ian S. Johnston, Q.C.
PRICE WATERHOUSE & CO.

55 Yonge Street
TORONTO 1
July 5, 1961.

Personal

C. H. Day, Esq.,
Elgin Handles Ltd.,
21 Kains Street,
St. Thomas, Ontario.

Dear Mr. Day:

With reference to our telephone conversation on Friday last I am enclosing a copy of the preliminary draft of a memorandum for the shareholders of C. Smythe, Limited setting out possible means of reorganization which we believed might be useful for the three main shareholders of C. Smythe, Limited. This memorandum was discussed at some length in a meeting with Messrs. Conn and Stafford Smythe; Mr. Ian Johnston, Q.C., also attended throughout the meeting.

At present the Smythes do not wish to take any steps to implement such a reorganization. Mr. Conn Smythe feels that the present arrangement is satisfactory and Mr. Stafford Smythe believes that the cost of $150,000 for income taxes and other items is too great for the benefits to be achieved This, of course, is a matter of opinion and since the shareholders are the ones who bear the cost, naturally we accept their views on the matter.

During the meeting with the Smythes I mentioned that there were two methods talked about in current tax literature whereby undistributed earnings of a company could be distributed tax free but that I was very reluctant to recommend such methods since I felt that they might be successfully attacked by income tax authorities, in which case the ultimate cost to individual shareholders would be considerably greater.

In the discussions I also pointed out that the question of undistributed income and designated surplus of corporations had been mentioned in the 1961 budget address of the Minister of Finance but he indicated that the whole matter was still under consideration and that the Government had come to no conclusions on how this rather difficult problem, particularly with respect to successful private companies, was to be dealt with. I had heard rumours before the budget address that some basis of withdrawing undistributed income from private corporations might be included in 1961, perhaps a flat rate of 15%. I also heard unsupported rumours that tax might be eliminated on such distributions. Certainly any step which would simplify the distribution, even at a 15% rate, would be cheaper for the shareholders than the methods outlined in the enclosed memorandum. On the other hand, taxes on the distribution of accumulated earnings might be increased. In view of the uncertainty it is difficult

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for us to advise a specific course of action too strongly but we feel that the possibilities should be considered periodically by the individual shareholders in the light of their personal circumstances.

Naturally Mr. Conn Smythe is concerned about his own personal estate planning and during our recent meeting he stated that the following arrangements had been made orally between the three major shareholders of C. Smythe, Limited, viz.:

1. In the event that Mr. Conn Smythe died, C. Smythe, Limited would arrange to purchase all shares of Maple Leaf Gardens Limited owned by him personally at fair market value at date of death in order to put Mr. Smythe's estate in funds to pay estate tax and succession duties. To do this C. Smythe, Limited would probably have to raise a loan with the shares as security or place a mortgage on the Caledon property. It is likely that interest on money borrowed specifically to buy shares of Maple Leaf Gardens would not be allowed for income tax purposes; on the other hand, an arrangement might be worked out in such a way that the interest would be allowed.

   At the meeting the possibility of paying more than the quoted market value was suggested since, by acquisition of all the shares, C. Smythe, Limited would have effective control of Maple Leaf Gardens Limited and the shares might properly be worth more than quoted market. I believe that this might be undesirable from an income tax standpoint since the excess between such a price and quoted market value might be deemed to be a benefit to a shareholder, viz. Mr. Smythe's estate.

2. In the event of your death, Mr. Smythe stated that either he or Stafford would arrange to purchase the shares of C. Smythe, Limited now owned by you from your estate at fair value. The suggestion was made that fair value might be that determined for estate tax and succession duty purposes but, on further reflection, I am inclined to think that such a fair value should probably be determined along the following lines:

   Net book value of C. Smythe, Limited plus excess of market value of marketable securities over book value plus excess of appraised value of Caledon land over book value.

   This matter should be considered further before any final arrangements are made.

3. In the event that Stafford Smythe died, Conn Smythe would buy the shares of C. Smythe, Limited now owned by Stafford Smythe from his estate at fair value.

During our discussions on Thursday I told the Smythes that any such arrangement should be in the form of a written agreement between the three main shareholders in order that their heirs would be adequately protected. This is most important both for the heirs and for the remaining shareholders since the remaining shareholders will be dealing with executors rather than with the individuals who discussed and agreed upon the original arrangements.

As arranged in our telephone conversation, you are to review the memorandum and the other matters outlined in this letter and consider them with your own financial adviser. I would hope that by the end of September final legislation in respect of the 1961 budget resolutions will have been enacted and at that time perhaps we could discuss the matter further when you are in Toronto.

As you know, I expect to be out of the country for several weeks but if you should have any immediate questions in connection with the matters referred to in this letter you could reach me by telephone on July 6.

Yours sincerely,
S. E. V. Smith

Enc.-Draft memorandum

On November 3, 1961, Mr. I. S. Johnston, Q.C., solicitor for Mr. Conn Smythe, in connection with drawing his will and implementing an estate plan for him, wrote him and in that letter advised that for liquidity of his estate, the reorganization of C. Smythe Limited was a major problem for future discussions (see Exhibit A-4). That letter in relevant part reads as follows:

3rd November, 1961.

PERSONAL:

Conn Smythe, Esq.,
President,
Maple Leaf Gardens Limited,
Carlton and Church Streets,
TORONTO 2, Ontario.

Dear Conn,

I enclose an outline of a Will in accordance with the instructions you gave me the other day.

. . .

This new Will will certainly simplify administration on the distribution of capital. However, it will not simplify the question of raising money for tax. The problem is that there is insufficient money in the free estate to pay the tax. I enclose a new Estimate of Estate Tax. This estimate presumes that the gift of 4,000 shares of Maple Leaf Gardens will be complete, the Lake Simcoe house is taken out of specifics, $16,000 added to free assets and Income Tax on the horses will be allowed as a deduction for Estate Tax.

The old problems are still there. Insufficient free assets for tax purposes. C. Smythe Limited will have to distribute $25 to get $13 for your estate. To get money out of C. Smythe Limited, Income Tax will have to be paid on the undistributed income on hand and the amount of Income Tax will be included in your estate for Inheritance Tax purposes.

A reorganization of C. Smythe Limited is a major problem for future discussion.

. . .

I have spoken to Mr. Smith and we would like some further discussion with you.

ISJ·MC
Encls.
cc: Mr. S. E. V. Smith.

Yours sincerely,
(I. S. Johnston)

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Then between November 17, 1961 and December 14, 1961, certain action was taken by the directors and shareholders of C. Smythe Limited in reference to obtaining for the shareholders a distribution to them of some of the said undistributed earned surplus of $728,652.

On November 17, 1961, (as mentioned earlier in these Reasons) at a meeting of the directors of C. Smythe Limited, it was "moved by Mr. C. Stafford Smythe, seconded by Mr. Day and unanimously carried, that the President be empowered to instruct the Managing Director, in consultation with Price Waterhouse & Co. to proceed immediately to arrange for the distribution of $375,000 to the shareholders of C. Smythe, Limited".

(This was made possible as mentioned above, because C. Smythe Limited had put in liquid form some of its assets and took further steps in this connection, *viz*; at this meeting, the directors authorized the sale of stock in Maple Leaf Gardens Limited to C. Stafford Smythe for $800,000 and prior to that they had authorized the sale of certain of the depleted gravel pits C. Smythe Limited owned.)

This direction of the directors in relation to part of the said undistributed earned surplus of C. Smythe Limited was in essence to implement the essential part of the plan of Mr. S. E. V. Smith of Price Waterhouse & Co. suggested on June 28, 1961, which as above noted involved the following matters:

(a) that a new company be incorporated;

(b) that the assets of the old company be sold to a new company;

(c) that the shareholders of the old company sell their shares to a dealer in securities;

(d) that the financing to enable the shares of the old company to be sold, be effected by obtaining "daylight" accommodation from the Bank (Mr. Smith said it could be as short as one minute);

(e) that there be a simultaneous exchange of cheques or drafts between the purchaser of the shares of the old company from its shareholders;

(f) that the security dealer's gross profit be the difference in price between the monies he obtained in C. Smythe Limited, the old company, and the amount he paid for the shares of the old company, less the taxes he would be required to pay under the provisions of section 105B of the *Income Tax Act*;

(g) that the shareholders of the old company reinvest the monies they obtained from the sale of their shares in the old company, in common shares and preference shares and debentures or other forms of loans in the new company; and

(h) that the business without interruption be carried on by the new company.

On the direction of Mr. Conn Smythe the security dealer chosen with whom it was proposed to deal was Greenshields Inc., with head office in Montreal, Quebec. This choice was made by Mr. Conn Smythe because of some World War II association he had with one of the latter's partners, a Mr. Tafts.

(Under this plan, it should be again noted, it was proposed that C. Smythe Limited pay the income tax required pursuant to the provisions of section 105B.

However, as also noted, this was not done, and the plan was slightly changed and Mr. Smith later advised the transaction that was entered into with the two Vancouver-based companies, F. H. Cameron Limited and Dabne Enterprises Limited, and no income tax was paid by C. Smythe Limited pursuant to section 105B of the *Income Tax Act*, or personally by any of the appellants or A. M. Boyd.)

On November 29, 1961, Mr. Smith, in carrying out the request of the directors pursuant to their said resolution of November 17, 1961, discussed with the shareholders of C. Smythe Limited the methods of getting out $375,000 to them; and on the same date, Mr. I. S. Johnston, Q.C., was instructed that he would be retained as solicitor in the reorganization of C. Smythe Limited necessary for this purpose.

On December 7, 1961, Mr. Smith advised Mr. Conn Smythe, President of C. Smythe Limited by letter (see Exhibit A-6) that the income tax cost of distributing the $375,000 would be $102,000 but that the shareholders would still be unable to withdraw "the realized and unrealized capital gains of about $1,800,000 ... without paying tax

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on the balance of the accumulated earnings" (i.e. the balance after subtracting $375,000 from $728,652) of the company.

He said "since the remaining accumulated earnings amount to about $300,000, it would probably cost another $100,000 to free the capital gains in the next year or two . . . ".

(It should be noted that in doing what was eventually done here—eliminated a tax cost to the company estimated by Mr. Smith of over $202,000.)

Mr. Smith then recommended the sale of assets to the new company, and the subsequent sale of shares of the old company to a broker at a cost to the company of approximately $150,000 (being approximately $48,000 of other costs, *viz.*, of accountants, solicitors, incorporations, etc., which added to the income tax cost of $102,000 payable under section 105B of the *Income Tax Act* brought the total estimated costs to about $150,000); and Mr. Smith stated that under this plan the shareholders of C. Smythe Limited would receive $2,117,580 in non-interest-bearing debentures, 10,000 shares in the new company and cash in the sum of $275,000, and in respect to the receipt of these three things the said shareholders would pay no personal income tax.

The said letter of Mr. Smith of December 7, 1961 to Mr. Conn Smythe reads as follows:

PRICE WATERHOUSE & CO.

55 Yonge Street
TORONTO 1

December 7, 1961.

Confidential

Mr. Conn Smythe, President,
C. Smythe, Limited,
899 Jane Street,
Toronto 9, Ontario.

Dear Mr. Smythe:

In accordance with the directors' resolution of November 16, 1961 you have asked our advice on the best method of making a cash distribution of $375,000 to the shareholders.

Among the ordinary methods of distribution a combination of cash dividends and a Section 105 election is the most economical in the circumstances. However, even if this method is used a distribution of $375.000 by March 1962 would involve a tax cost of about $100,000 (see Schedule A). Despite this substantial outlay in tax, the realized and unrealized capital gains of the company of about $1,800,000 could still not be withdrawn without paying tax on the balance of the accumulated earnings. Since the remaining accumulated earnings amount to about $300,000, it would probably cost another $100,000 to free the capital gains in the next year or two and the tax cost would gradually increase as profitable operations added to the accumulated earnings.

Under these circumstances we strongly recommend that you adopt a different course of action which, for the expenditure of about $150,000, will make all the accumulated earnings and capital gains of the company to date available to the shareholders without payment of further tax. Under the proposed plan, the assets of the present company would be sold to a new operating company owned by the shareholders of C. Smythe, Limited and the shareholders would then sell their shares of C. Smythe, Limited to a dealer in securities for a price which, in the aggregate, would be $150,000 less than their equity. A dealer in securities would be able to pay this price for the shares since, under Section 105B of the Income Tax Act he could have the company's assets distributed at a tax cost equal to 16⅔% of the accumulated earnings. The principal result of the reorganization would be that the shareholders would replace their common shares of C. Smythe, Limited with debentures (and shares) of a new operating company; such debentures could be redeemed free of tax when funds were available and not needed for the new company's operations.

A detailed outline of the proposed plan is set out on Schedule B attached, along with a pro forma balance sheet showing the position after the reorganization. In this outline we have assumed that the Jane Street properties would be sold to the new company at fair market value, which has been taken as $250,000. On the basis of our conversations with you we understand that the shareholders are to receive the same amount as if a cash distribution of $375,000 had been made by the company, viz. $275,000 after taxes. Under the proposed plan this distribution would be accomplished since the shareholders of C. Smythe, Limited would hold the following assets instead of their present holdings in C. Smythe, Limited:

		Securities of a new operating company	
	Cash	Non-interest bearing debentures	Common stock
Conn Smythe	$ 143,000	1,101,141	5,200
C. Stafford Smythe	84,700	652,215	3,080
C. H. Day	44,000	338,813	1,600
A. M. Boyd	3,300	25,411	120
	$ 275,000	2,117,580*	10,000

*Based on unaudited financial statements at October 31, 1961 and adjustments referred to on Schedule B.

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You will note from the pro forma balance sheet in Schedule B that the new operating company would have cash and liquid assets of $1,197,880 in addition to other working current assets which exceed its liabilities. If it were decided to distribute some of these funds or some of the funds produced by future operations of the new company, non-interest bearing debentures could be redeemed pro rata and the proceeds received tax free by individual shareholders.

In order to provide funds for the estate of a deceased shareholder an agreement could be entered into among the shareholders whereby in the event of any shareholder's death, debentures held by his estate would be redeemed in the following annual amounts:

Conn Smythe	$ 26,000
C. Stafford Smythe	15,400
C. H. Day	8,000
A. M. Boyd	600

This would be in addition to any pro rata distribution of cash earnings; presumably the agreement would also provide that no distributions would be made which would jeopardize the company's ability to make the specified annual redemptions of debentures held by a deceased shareholder's estate.

We believe that the arrangement outlined in general above and in somewhat more detail in Schedule B would be in the best interests of all the shareholders and we strongly recommend that it be adopted. If the shareholders do decide to go ahead with the plan we believe that it should be completed before February 28, 1962. The specific actions to be taken are numerous (see Schedule C), and accordingly a decision should be made as soon as possible.

Undoubtedly you will wish to have the company's solicitor consider the plan and its ramifications and the necessary documents required to implement the proposed reorganization.

If you or any other shareholder would like to discuss this plan further with us we shall be pleased to do so.

Yours very truly,
(S. E. V. Smith)

Enc.-Schedules

Schedule A

C. SMYTHE, LIMITED

CALCULATION OF INCOME TAXES AND NET PROCEEDS TO SHAREHOLDERS FROM A $375,000 DISTRIBUTION BY THE COMPANY

	Gross distribu-tion	Less income taxes	Net to share-holders
Cash dividends:			
Before December 31, 1961	$ 93,750	37,012	56,738
After December 31, 1961 and before February 28, 1962	93,750	37,012	56,738
	$ 187,500	74,024	113,476
Section 105 distribution:			
After February 28, 1962	187,500	28,125	159,375
	$ 375,000	102,149	272,851
		Taken as	$ 275,000

Net proceeds to shareholders after all income taxes (see Note):		
Conn Smythe	$ 136,200	
C. S. Smythe	88,400	
C. H. Day	46,700	
A. M. Boyd	3,700	
		$ 275,000

NOTE: The above calculations are based on estimates of the shareholders' taxable incomes.

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Schedule B

C SMYTHE, LIMITED

PROPOSED REORGANIZATION OF COMPANY'S OPERATIONS

1. Form a new operating company, C. Smythe For Sand Limited, with an Ontario charter and a capitalization of, say, 40,000 common shares at $1 00 per share.

   Present shareholders of C. Smythe, Limited would subscribe for shares in the new company for cash in exactly the same ratio as their present holdings in C. Smythe, Limited, viz :

Conn Smythe	5,200
C. Stafford Smythe	3,080
C H Day	1,600
A. M. Boyd	120
	10,000

2. C. Smythe, Limited would sell the following assets to C. Smythe For Sand Limited:
   (a) All cash except $435,000 required for cost of reorganization and cash requirements of shareholders
   (b) All Caledon sand and gravel mines, buildings and other fixed assets at book value which is equivalent to undepreciated capital cost.
   (c) All other Caledon operating assets, including cattle, accounts receivable, etc., at fair market value.
   (d) 10,000 shares of Maple Leaf Gardens Limited at $300,000 (the option price, which equals fair market value).
   (e) Other marketable securities at fair market value which approximates book value.
   (f) The mortgage receivable on Jane Street property at book value, which is fair market value.
   (g) The fully depleted sand and gravel properties at Jane Street at fair market value (taken as $250,000 in present calculation).
3. C. Smythe For Sand Limited will assume all liabilities of C. Smythe, Limited.
4. C. Smythe For Sand Limited will issue non-interest bearing debentures for the net assets taken over from C. Smythe, Limited.
5. The shareholders of C. Smythe, Limited would sell their shares to a dealer in securities at a price which would be equivalent to the shareholders' equity in C. Smythe, Limited (after taking into account capital gains on all dispositions of Jane Street property and investments in common stocks) *less* income taxes and other costs arising from the reorganization, which are estimated to be $150,000.

A pro forma balance sheet of the new operating company based on unaudited figures as of October 31, 1961 as supplied by the company's accountant, taking into account the above transactions and the sale to outsiders of 20,000 shares of Maple Leaf Gardens Limited at 40¢ per share for cash, is set out below:

C. SMYTHE FOR SAND LIMITED

(a new company)

ASSETS

Cash and Other Liquid Assets:		
Cash	$ 585,600	
10,000 shares of Maple Leaf Gardens Limited at $30 each	300,000	
Investment in stocks and bonds at market value	171,080	
Mortgage due on Jane Street property	131,200	
Subscriptions on capital stock due from shareholders	10,000	$ 1,197,880
Other Current Assets:		
Trade and other receivables	$ 173,700	
Due from Conn Smythe Contracting Company Limited	31,200	
Cattle inventory	35,300	240,200
		$ 1,438,080
Mortgage Receivable		24,000
Jane Street Properties, at estimated realizable value		250,000
Fixed Assets:		
Caledon and other operating assets, at cost less depreciation		541,700
		$ 2,253,780

LIABILITIES

Current Liabilities:		
Accounts payable and accruals	$ 67,100	
Provision for income taxes	5,100	$ 72,200
Mortgages Payable		54,000
Non-interest Bearing Debentures		2,117,580
Capital Stock:		
10,000 common shares of $1 each		10,000
		$ 2,253,780

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A pro forma balance sheet of C. Smythe, Limited shortly before completion of its sale to an outsider is set out hereunder:

ASSETS

Cash for distribution of shareholders		
To be retained		$ 275,000
To be reinvested by shareholders in common stock of C. Smythe For Sand Limited, a new operating company		10,000
Cash for income taxes and other costs of reorganization		150,000
		$ 435,000
Non-interest bearing debentures of C. Smythe For Sand Limited		2,117,580
		$ 2,552,580

SHAREHOLDERS' EQUITY

Common shares		$ 25,000
Premium on common shares		6,000
Capital gains (Note 1)		1,840,380
Accumulated earnings:		
Balance at February 28, 1961	$ 644,003	
Earnings for eight months ended October 31, 1961 (Note 2)	37,197	681,200
		$ 2,552,580

NOTES:

1. Capital gains are made up of the following items:

Sale of fully depleted gravel properties	$ 789,200	
Sale of investments in common stocks	104,300	
Sale of 20,000 shares of Maple Leaf Gardens Limited at $40 per share	531,253	
	$ 1,424,753	(Realized)
Sale to C. Smythe For Sand Limited of—		
(a) 10,000 shares of Maple Leaf Gardens Limited at $30 per share	$ 165,627	
(b) Jane Street properties at	250,000	
	$ 415,627	(Unrealized)
	$1,840,380	

2. The above amounts are based on unaudited figures at October 31, 1961.

Immediately before the sale of C. Smythe, Limited to an outsider, the shareholders would buy for cash the non-interest bearing debentures of $2,117,580 from the company. The selling price of the shares of C. Smythe, Limited to the outsider would then be $2,402,580 cash, and the shareholders would net $285,000 in cash, viz. $275,000 distribution and $10,000 to be reinvested in the new company.

Schedule C

C. SMYTHE, LIMITED
ACTIONS TO BE TAKEN AND TENTATIVE
TIMETABLE FOR PROPOSED REORGANIZATION

To do	*To be done by*	*Date to be completed*
1. Call special meeting of shareholders to approve reorganization	President	December 8
2. Incorporate new company	Company solicitor	Incorporation date December 12
3. Close books of C. Smythe, Limited and open books of new company as of incorporation date	Company accountant	December 12
4. Subscription for shares of new company	C. Smythe .... 5,200 C. S. Smythe .. 3,080 C. H. Day ..... 1,600 A. M. Boyd 120	December 15
5. Calculation of undistributed income of C. Smythe, Limited as at February 28, 1961	P. W.	December 15
6. Appraisal of Jane Street property	Company officials and appraisor	December 15
7. Draw up agreement for sale of assets of C. Smythe, Limited to new company as of date of incorporation of latter company	Company solicitor in collaboration with P.W.	December 15
8. Negotiation with a dealer in securities to settle fee and other details re sale of shares of C. Smythe, Limited	P.W. subject to final confirmation by company officials	December 4 on
9. Approval of sale of assets of C. Smythe, Limited at special shareholders' meeting	Shareholders	December 22
10. (a) Audit of C. Smythe, Limited as of date of sale of assets	P.W.	January 26
(b) Preparation of final tax returns and completion of undistributed income for C. Smythe, Limited	P.W.	January 31

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To do	To be done by	Date to be completed
11. Completion of sale of assets of C. Smythe, Limited to new company, in return for debentures	Company officials and company solicitor in collaboration with P.W.	January 31
12. (a) Shareholders of C. Smythe, Limited purchase debentures of new company for cash	Shareholders and company solicitor in collaboration with P.W.	February 6
(b) Audited balance sheet of C. Smythe, Limited, showing cash and shareholders' equity	P.W.	February 6
(c) Sale of all shares of C. Smythe, Limited to dealer in securities	Shareholders and company solicitor in collaboration with P.W.	February 7
13. (a) File final tax returns and calculation of undistributed income of C. Smythe, Limited, reporting regular income for incomplete fiscal year 1961/2 and tax under Section 105B	Dealer in securities	February 8
(b) Distribution of remaining cash of C. Smythe, Limited to dealer in securities on winding up	Dealer in securities	February 8
14. After tax clearance has been obtained, wind up C. Smythe, Limited	Dealer in securities, solicitors and auditors	After February 8

On December 8, 1961, Mr. Smith got in touch with the said Mr. Tafts (the partner of Greenshields Inc., Mr. Conn Smythe had known) to find out whether that company would be interested in acting as such a dealer in securities under the proposals. Mr. Tafts told Mr. Smith that he was unfamiliar with this type of transaction and that he would take it up with his Montreal associates who had experience with these matters and advise.

Then on December 12, 1961, Mr. Campbell Leitch, a Montreal partner of MacDonald Currie and Co., the auditors for Greenshields Inc., called Mr. Smith and made a proposal that Greenshields Inc. buy the shares of C. Smythe Limited at book value less 5 per cent of undistributed income for resale to some other party or parties. Mr. Smith recommended this transaction to Mr. Conn Smythe.

But by December 14, 1961, it seemed apparent that no sale of the shares in C. Smythe Limited would be made to Greenshields Inc. because the latter had amended their proposals. Greenshields Inc., according to the evidence, wanted the vendor shareholders of C. Smythe Limited, prior to the sale of shares of it, to arrange for a stock split of its shares and also they wanted the closing of such sale by the end of the year (i.e. 1961). Mr. Smith advised against this sale because it was thought by him and Mr. Johnston that there was no "good business reason" for splitting the shares of C. Smythe Limited and if the present shareholders of it caused such to be done, such action might be considered by the income tax authorities to be part of a "winding-up, discontinuance or reorganization of its business", so that the then present shareholders (the appellants and Mr. A. M. Boyd) of C. Smythe Limited, pursuant to the provisions of section 81(1) of the *Income Tax Act* might be deemed to have received a dividend to the extent of their respective "portion of the undistributed income then on hand" of C. Smythe Limited. (see section 81(1)(*b*) of the Act.)

Mr. Smith put it this way in his evidence:

> MR. SMITH: Well, it would appear to me that they were asking us to countenance some type of transaction by the present shareholders, at least by the Smythe group then shareholders of C. Smythe Limited that might lead to the evasion of taxes eventually and we did not wish to have any part of it. It did not seem to us that there was any good business reason why we should split the shares of C. Smythe Limited to say one to ten, one to nine—I think it eventually got up to one to one hundred. And both Mr. Johnston and I advised that we could see no reason to carry this type of transaction out.

Then between December 15, 1961 and December 27, 1961, the following things took place:

On December 15, 1961 (Friday), a meeting of the Board of Directors of C. Smythe Limited authorized the sale to C. Smythe For Sand Limited of the former's assets pursuant to the terms of a Draft Agreement attached to the Minutes.

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On the same day, there was a purported meeting of the Board of Directors of C. Smythe for Sand Limited (an application for a charter for which had just been made that day to the Provincial Secretary of the Province of Ontario but which company was therefore still unincorporated) at which the Directors (1) authorized the allotment of 9,996 common shares of the company to the appellants for $9,996; (2) authorized the creation of non-interest-bearing debentures not exceeding $2,750,000 to mature December 15, 1981; and (3) approved the purchase of assets and undertaking of C. Smythe Limited as per Draft Agreement.

This Agreement between C. Smythe Limited and C. Smythe For Sand Limited was finally executed in the form as set out in Exhibit A-26 as follows:

MEMORANDUM OF AGREEMENT made as of the 15th day of December, 1961,

BETWEEN:

C. Smythe, Limited, hereinafter called "the Vendor",

OF THE FIRST PART

and

C. Smythe for Sand Limited, hereinafter called "the Purchaser"

OF THE SECOND PART

IN CONSIDERATION of the mutual agreements hereinafter contained it is agreed by and between the parties hereto as follows:

1. The Vendor agrees to sell and the Purchaser agrees to purchase all the undertaking, property and assets as a going concern of the Vendor as at the close of business on the 15th day of December, 1961, including the following:

(a) the goodwill of the said business with the exclusive right to represent the Purchaser as carrying on the same in continuation of and in succession to the Vendor and the right to use any words indicating that the business is so carried on;

(b) all trade marks, trade names, copyrights, trade designs, inventions and patents and licenses connected with the business of or belonging to the Vendor;

(c) all of the property of the Vendor moveable or immoveable, real and personal of every kind and wheresoever situate including freehold and leasehold property, leases and licenses owned or held by the Vendor;

(d) all the sand and gravel mines, buildings, improvements, plant, machinery, equipment, trucks, motors, waggons and horses, tools, utensils, inventory, stock-in-trade, supplies of every kind and nature owned by the Vendor;

(e) all of the book and other debts due or accruing due to the Vendor and the full benefit of all securities for such debts;

(f) the full benefit of all existing contracts and engagements to which the Vendor may be entitled;

(g) all cash on hand and in bank and all Bills and Notes owned by the Vendor;

(h) all shares, bonds and securities owned by the Vendor, including 10,000 shares of Maple Leaf Gardens Limited which are subject to an Option Agreement;

(i) all other property, assets and rights to which the Vendor is entitled in connection with its business or otherwise.

2. The Vendor shall take all proper steps, actions and corporate proceedings on its part to enable it to vest a good and marketable title in the Purchaser to the said business, property, assets and undertaking, and at the time of closing shall deliver to the Purchaser such deeds, conveyances, assurances, transfers, assignments and consents as Counsel for the Purchaser may require. And the Vendor will from time to time on reasonable request and at the expense of the Purchaser execute such further documents and assurances as may be necessary to assure the property and assets in the Purchaser. The Purchaser agrees to accept the title of the Vendor in all property and assets as such title will, stand at the date of closing.

3. The consideration payable by the Purchaser under this Agreement shall be the sum of $2,611,769.00 which is the difference between the aggregate value of the assets set out in Schedule "A" hereto and the aggregrate value of the liabilities set out in Schedule "B" hereto.

4. The Purchaser covenants to pay, satisfy, discharge, perform and fulfil all debts, liabilities, contracts and engagements of the Vendor incurred and/or arising on or before the date of closing the purchase and sale and to indemnify and save harmless the Vendor, its successors and assigns against all actions, proceedings, claims and demands in respect thereof including, without limiting the generality of the foregoing, all debts and liabilities of the Vendor not recorded on its books incurred and/or arising on or before the date of closing the purchase and sale.

5. The Vendor covenants with the Purchaser that the Vendor will cause to be prepared such Returns as may be required by The Income Tax Act of Canada and The Corporations Tax Act of Ontario for the fiscal period ending the 28th day of February, 1962, in such form and with such content in respect of operations for the periods ending on or before the 15th December, 1961 as may be acceptable to Messrs. Price Waterhouse & Co. The Parties agree that if the Minister of National Revenue or the Treasurer of Ontario shall assess a larger amount of tax than that shown on the original or amended Tax Returns of the Vendor in respect of the periods ending on or before the 15th day of December, 1961, then the Purchaser shall have the right to object and appeal any such assessment in the name of the Vendor.

6. The sale and purchase shall be closed in Toronto on the 28th day of December, 1961, or on such earlier or later date as shall be mutually agreed.

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7. The sale and purchase shall take effect as at the closing of business on the 15th day of December, 1961, from which time until the closing of the sale and purchase the Vendor shall be deemed to have carried on its undertaking and business for and on behalf of the Purchaser, and the Purchaser shall be entitled to all income and profits in connection therewith during the said period. And the Vendor warrants and agrees that until the closing of the sale the Vendor's business shall continue to be carried on in its usual and ordinary course, and that the Vendor shall not declare or pay any dividends or make any payments except such as are necessary for the ordinary conduct of its business, including wages and salaries to employees and officers at the rates heretofore prevailing.

8. All books of account of the Vendor, all books of reference to customers, and all documents and data of the Vendor or in its possession or control relating to the business of the Vendor shall, on closing, be delivered to the Purchaser which shall henceforth be entitled to the custody thereof. The Purchaser covenants to retain such books and documents as required by the Income Tax Act and will make them available to the Vendor upon reasonable request. The Vendor shall retain possession of the Corporate Seal, Stock Ledger and Transfer Book, and the Company's Minute Books. It is agreed that after the date of closing the Purchaser or its agent shall have access to the Company's Minute Books covering the period prior to the date of closing and shall be entitled to make copies or excerpts therefrom.

9. The Vendor shall forthwith after the closing of the sale and purchase cease to carry on the business of producing sand and gravel and dealing in and using construction materials in the Province of Ontario.

10. The Vendor hereby undertakes to make application to the Provincial Secretary of Ontario for permission to change its name to any name acceptable to the Lieutenant-Governor of Ontario which does not include the name "Smythe", such application to be made within thirty days of the closing of the transaction, or in the alternative, to distribute its assets and make application to the Provincial Secretary of Ontario for surrender of its Charter, such application to be made within sixty days of the closing of the transaction.

IN WITNESS WHEREOF the parties hereto have executed this Agreement under the hands of their duly authorized officers in that behalf this 28th day of December, 1961.

C. SMYTHE, LIMITED
per: Conn Smythe
per: A. M. Boyd

C. SMYTHE FOR SAND LIMITED
per: Conn Smythe
per: A. M. Boyd

SCHEDULE "A"

SUMMARY OF ASSETS SOLD BY C SMYTHE, LIMITED TO C. SMYTHE FOR SAND LIMITED AS OF DECEMBER 15, 1961

Description	*Amount*
Cash on hand .... $	7,031
Bank balances and accrued interest	188,126
Time deposit due January 2, 1962 at guaranteed principal amount and accrued interest	800,945
Marketable securities (including 10,152 shares of common stock of Maple Leaf Gardens Limited) at fair market value	475,279
Trade accounts receivable at book value, less allowance of $10,000 for doubtful accounts	181,694
Amount receivable from Conn Smythe Contracting Company Limited at book value	29,773
Amounts receivable from employees and others	1,215
Income tax refund receivable from the Department of National Revenue	2,500
Inventory of feeder cattle at fair market value	108,661
Prepaid insurance and realty taxes	2,896
Mortgage receivable from Vodan Investments Ltd. at principal amount and accrued interest	128,320
Caledon sand and gravel mine at book value	339,528
Caledon plant parking area construction at net book value ..	1,000
Caledon cement silo at net book value	2,362
Caledon frame buildings and fences at net book value	12,668
Caledon equipment and other tangible capital assets not otherwise specified at net book value	5,626
Caledon buildings and mining machinery and equipment acquired for the purpose of gaining or producing income from a mine, contractor's movable equipment, movable farm equipment, wagons, trailers, automotive equipment, etc. at net book value	223,764
Jane Street, Toronto, sand and gravel mine at fair market value	250,000
Jane Street, Toronto, building acquired for the purpose of gain or producing income from a mine	1
Goodwill	1
	$ 2,761,390

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SCHEDULE "B"

SUMMARY OF RECORDED LIABILITIES OF C. SMYTHE, LIMITED ASSUMED BY C. SMYTHE FOR SAND LIMITED, AS OF DECEMBER 15, 1961

Trade accounts payable	$	52,246
Accrued liabilities		40,856
Amount payable to Roseland Homes Limited		2,519
Mortgages payable—principal amount		
John L. Kestle		10,000
Melvin Lundy		4,000
Mrs. I. M. Krouse		10,000
F. N. Braiden		30,000
	$	149,621

After this meeting on December 15, 1961, Mr. Conn Smythe asked Mr. Smith to contact Greenshields Inc. again to ascertain "whether or not it would act as a dealer in securities under the original proposal" and Mr. Smith did; but Greenshields Inc. declined to enter into a contract in this fashion. Mr. Smith communicated this information to the shareholders of C. Smythe Limited on Friday, December 15, 1961 "with the suggestion that I would reconsider the possibility of adopting other methods of dealing with the problem although I had previously told 'A' (Mr. Conn Smythe) that I did not recommend devious methods." (See Exhibit A-41.)

Then on Monday, December 18, 1961, Mr. Smith sought legal advice for his firm, Price Waterhouse & Co. in this matter and consulted Mr. Stuart Thom, Q.C., of Toronto. One of Mr. Smith's stated reasons for so doing, was "the possibility that I should consider on my client's behalf devious methods suggested in current tax literature for dealing with private companies with undistributed income on hand . . ." (see Exhibit A-41).

At this consultation, Mr. Smith asked the following questions and received the answers following, according to a memorandum which was, according to Mr. Smith "prepared on January 2, 1962 in case I ever needed to refresh my memory on the matter at some later date".

(See Memorandum, Exhibit A-41.) The relevant part of this memorandum reads as follows:

1. In his opinion would there be anything improper, having reference to section 138 of the Income Tax Act, in having "X"'s shares sold to a dealer in securities, the dealer paying the 20% tax on undistributed income and then winding up the company?

   Thom indicated that in his opinion this action was provided for in the Income Tax Act and that it was perfectly straightforward and acceptable to the income tax authorities.

2. I then asked Thom if the proposal from Greenshields whereby the shareholders of "X" would sell their shares for a fixed price determined at net book value of the company less 5% of undistributed income could, in his opinion, involve the shareholders of my client in any action or publicity under Section 138 or other sections of the Income Tax Act.

   Thom informed me that there was no section of the Income Tax Act which provided for a tax on undistributed income of a company or on its shareholders until such time as they decided to distribute such income. Obviously the shareholders of "X" could defer paying tax indefinitely and under the Greenshields' proposal presumably the purchaser was either arranging for an indefinite deferment of tax or no tax. In view of all the circumstances, Thom was of the opinion that the shareholders of "X" could not be successfully attacked on any grounds for selling their shares at the best possible price they could get.

3. I then asked Thom if the shareholders arranged to have "X"'s shares split, say in a ratio of nine non-voting to one voting, in order that they might sell their shares, whether he would consider that there was anything improper in the transaction.

   Thom informed me that although this was not quite as clear as 2 above, after all common shares are frequently split and if this was a condition of the purchaser before he would acquire the shares, then presumably it was reasonable for the shareholders of "X" to do so in order to get the best price for their shares and he doubted if anyone could successfully attack the transaction.

4. In view of the fact that many suggestions for withdrawing undistributed income or "dividend stripping" are mentioned in tax literature, I asked Thom what would be the position of "X"'s shareholders, or my position, if they, or I on their behalf, went out and solicited several brokers in order to find two or more who would each buy less than 50% of the shares of "X" and thus be able to take out dividends without paying the tax required under Section 105B.

   Thom informed me that this might well be considered an endeavour to evade tax that might otherwise be payable under the Income Tax Act and thus might fall under Section 138. He also called my attention to Section 132 which says, in part—"Every person who has........wilfully, in any manner, evaded or attempted to evade, compliance with this Act or payment of taxes imposed by this Act,........is guilty of an offence" and, in brief, may be subject to a fine not exceeding $10,000 and a term of imprisonment not exceeding two years.

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> In addition to the possibility that my clients, the brokers or I might be considered as conspiring to evade taxes, the brokers might well be considered to be not acting at arm's length, in which case control of "X" would be acquired by a group and the undistributed income at the beginning of the year deemed to be designated surplus taxable on distribution at ordinary corporate rates.
>
> In view of the foregoing advice I discarded any thought of promoting any devious methods of dealing with undistributed income or "dividend stripping".

At this discussion also, Mr. Smith said he considered with Mr. Thom a letter of proposal to a Mr. Joseph Tenanbaum, President of Runnymede Steel Construction Company, Toronto, dated December 5, 1961, which company was a mutual client of Mr. Thom's firm and Price Waterhouse & Co. This letter concerned the possibility of selling shares of a private company at book value less 5 per cent of undistributed income. A copy of this letter to Mr. Tenanbaum is Exhibit A-42 and reads as follows:

December 5, 1961.

Mr. Joseph Tenanbaum,
Runnymede Steel Construction Company Limited,
3471 Dundas Street,
Toronto, Ontario.

Dear Sir:

Because we are solicitors for one of a group of investors we have been asked to write to you. These investors are interested in the purchase of all of the shares of your Company. They understand that your Company has sold all its assets to Dominion Bridge Company Limited retaining only cash and some property. They are prepared to pay cash for the shares.

Our clients understand that the surplus of your Company exceeds $1,000,000.00 and they will purchase on the basis of dollar for dollar on capital and 95 cents on the dollar for surplus (undistributed income).

Our clients believe that you may intend to retain the shares of Runnymede Steel Construction Company Limited and ask you to consider the advantages which would accrue to you in the elimination of its corporate surplus. They can suggest a pattern whereby this elimination might be carried out by you in a practical manner.

Our clients propose that you form a new Company known as Runnymede Steel Construction 1961 Limited or any name you prefer and that you change the name of the present Company to R.S.C. Enterprises Ltd. Then you can cause the old Company, R S C. Enterprises Ltd. to sell all of its business and assets to the newly incorporated company for a note or a note and preference shares.

At this point the balance sheet of the new company would show assets being all of those assets transferred from the old Company with liabilities being a note payable to the old Company, capital as you may wish to establish it and all surplus. The old Company's balance sheet would show assets being a note or a note and preference shares with liabilities being only capital and surplus.

You will wish to discuss with your advisors the advantages which can accrue in the establishment of such a new Company. They will quite likely wish to organize it in a way which will bring to you advantages in estate planning and particularly the minimisation of taxation.

Having re-organized you would cause the new Company to borrow sufficient monies to pay off its note to redeem its preference shares if any from the old Company and this would transfer the indebtedness of the new Company from the old Company to the bank. It would place the old Company in a fully liquid position with all of its assets being cash. With the old Company in this position my clients would pay you cash for all of the shares of the old Company.

Actually your borrowings from the bank in the new Company need only last for a half-hour to a one-hour period because the sale of shares of the old Company would place cash in the vendor shareholders' hands which they would in turn immediately advance to the new Company. The new Company would then be in a position to retire its bank loan.

Notice that you would then be in a position to withdraw any sum of money you wished from your new Company because of its liquid position. You would be able to make withdrawals free of personal income tax to the full amount of the shareholders' loan and the capital of your new Company.

Our investor clients would use the Company which they purchased for investment purpose. They do not in a short time liquidate such Companies but maintain them over a period of years making use of investment powers.

Our clients would be pleased to have this matter discussed at greater length with your solicitors or your chartered accountants. They regret that time within this year is short but suggest that the feasibility of this transaction should be established as early as possible. It would be desirable, if you are interested, to complete such a transaction prior to December 31st of this year.

Yours truly,

DOUGLAS, SYMES & BRISSENDEN,
Per

WJT/mm

Mr. Smith had previously heard of this proposal and on Tuesday, December 19, 1961, made further inquiries from Mr. J. H. M. Woods, a partner of his, of Price Waterhouse & Co. who was dealing with the matter of Mr. Tenanbaum and Runnymede Steel Construction Company Limited.

Apparently the day previous Mr. Wood had spoken with Mr. A. D. Russell, a Vancouver partner of Price Waterhouse & Co., and a reputed tax specialist, in a conference call with the representative of the prospective purchaser

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and his solicitor, but Mr. Tenanbaum was not interested in this proposal. Mr. Wood had sent to Mr. Russell a copy of this Tenanbaum letter.

In the afternoon of December 19, 1961, Mr. Smith telephoned Mr. Russell in Vancouver and asked him to make inquiries as to the reputation of the solicitors who wrote this so-called said "Tenanbaum letter" namely, Douglas, Symes & Brissenden, and also of Mr. F. H. Cameron who was the representative of the purchaser.

(In this connection, as appears from the evidence of Mr. Russell taken on commission in Vancouver, B.C., which questions and answers were put to Mr. Russell at this trial when he was called as a witness, Mr. Russell knew that Mr. Cameron was what colloquially was referred to at the time as a "dividend stripper". The questions and answers were as follows:

Q. Did you know that Cameron purchased a great many of the companies for the sake of obtaining the surplus out of the company?

A. I knew he was in the business but I didn't know how extensive it was.

Q. But you knew he was in that business?

A. Oh yes, it was common knowledge.

Q. As far as you know, have Price, Waterhouse in Vancouver had any other similar dealings to this?

A. Not to my knowledge. I was the only tax partner at that time and I have had no part of any such transactions . . .

Q. The Commissioner: To the best of our knowledge Price, Waterhouse has not been in any other than this one.

A. That is my understanding too, and I personally wasn't too happy about this. We certainly did not go out and advocate this type of transaction or promote it with our clients at all.)

Mr. Russell reported to Mr. Smith what he had ascertained as a result of the inquiries he made following this request, whereupon Mr. Smith asked Mr. Russell to find out if Mr. Cameron would be interested in making a proposal similar to that made to Tenanbaum (as contained in the above mentioned letter).

Mr. Russell called Mr. Cameron and later that day Mr. Cameron telephoned Mr. Smith to tell him that he was interested. Mr. Cameron told Mr. Smith also that he would wish such a transaction closed before December 29, 1961. Mr. Smith then inquired as to how soon Mr. Cameron would have to know the precise final amount payable for completing the transaction, and also two other matters which are important.

The two other matters discussed in my view in this telephone conversation between Mr. Smith and Mr. Cameron were as follows; and about them there was a reluctance on the part of Mr. Smith to admit in the witness box; and in respect to them in the argument on summing up there were different views submitted by opposing counsel.

Mr. Smith made notes at the time of this telephone conversation with Mr. Cameron (See Exhibit R-52; and such should be compared with the Tenanbaum letter (Exhibit A-42) especially the first and last paragraphs of it as to which specifically Mr. Smith made these notes in his memorandum reading:

"first paragraph" and "second last paragraph".)

The first paragraph of the Tenanbaum letter (Exhibit A-42) states that the solicitors represent and act for a group of "investors" who are interested in the purchase of all of the shares of Mr. Tenanbaum's company.

The second last paragraph of this letter says that these client "investors" "do not in a short time liquidate such companies but maintain them over a period of years making use of investment powers".

Following this, Mr. Smith again called Mr. Thom on the telephone and asked him for his opinion on the sale of the shares in C. Smythe Limited to a group of investors in Vancouver. Mr. Thom said he would consider the matter and let Mr. Smith know by noon December 20, 1961.

Later on that evening Mr. Cameron again spoke on the telephone to Mr. Smith and again assured Mr. Smith that his group never liquidated companies. Mr. Smith asked "for confirmation of Cameron's proposal by night letter". Mr. Cameron agreed to this and said he would also have his solicitors confirm this information. (Reference to this telephone conversation and what was requested is contained in Mr. Smith's further notes—Exhibit R-52.)

On the next day, December 20, 1961, Mr. Smith received a night letter from Mr. Cameron advising Mr. Smith that they represented "a group of investors" who would purchase all the issued shares on the basis of "dollar for dollar on capital and nine-five per cent on undistributed income" (see Exhibit A-17).

Mr. Smith also received a night letter from the solicitors for Mr. Cameron's group, namely, Mr. Thompson of the

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legal firm of Douglas, Symes & Brissenden. Mr. Thompson confirmed that Mr. Cameron's group did not wind-up companies (see Exhibit A-18), but kept them in good standing and used "their investment powers".

These two night letters read as follows:

A CANADIAN PACIFIC

TELEGRAM

1961 DEC 20 AM 1 13

FD VANCOUVER BC 19

MR S E V SMITH

PRICE WATERHOUSE AND CO 55 YONGE ST TORONTO ONT

WE UNDERSTAND THAT YOU HAVE AN UNDISCLOSED CLIENT WHO OWNS A COMPANY WITH ASSETS BEING CASH NOT EXCEEDING THREE MILLION DOLLARS AND WITH ITS ONLY LIABILITIES BEING CAPITAL, SURPLUS PREMIUM ON SHARES AND WITH UNDISTRIBUTED INCOME OF NOT LESS THAN FIVE HUNDRED THOUSAND DOLLARS STOP WE REPRESENT A GROUP OF INVESTORS WHO ARE PREPARED TO PURCHASE ALL OF THE ISSUED SHARES OF THIS COMPANY FOR CASH AT DOLLAR FOR DOLLAR ON CAPITAL AND NINETY FIVE PER CENT ON UNDISTRIBUTED INCOME STOP WE DO NOT LIQUIDATE SUCH COMPANIES AND THIS COMPANY WILL BE MAINTAINED IN EXISTENCE AS A MEANS OF INVESTMENT AND WILL FILE ANNUAL TAX RETURNS AND PROVINCIAL REPORTS STOP WE UNDERSTAND THAT THE COMPANIES NAME WILL BE CHANGED PRIOR TO OUR PURCHASE OR WILL BE IN THE PROCESS OF BEING CHANGED AT THAT TIME F H CAMERON LTD

CN TELECOMMUNICATIONS

VANCOUVER B C 1961 DEC 20 AM 12 08

S E V SMITH, PRICE WATERHOUSE AND CO

55 YONGE ST TOR

RE: NIGHT LETTER FROM CLIENT FH CAMERON WHO REPRESENTS INVESTORS WHO PURCHASE SHARES OF COMPANIES WITH SURPLUSES. HIS OFFER WITH CONDITION THAT INVESTORS BE FULLY PROTECTED AS OUTLINED IS BONA FIDE. THE COMPANY WHOSE SHARES ARE TO BE PURCHASED WILL NOT BE LIQUIDATED FOR MANY YEARS. NO COMPANIES WITH SURPLUSES WHOSE SHARES HE HAS CAUSED TO BE PURCHASED AND WITH RESPECT TO WHICH WE HAVE ACTED FROM 1956 TO DATE HAVE BEEN LIQUIDATED. THEY ARE KEPT IN GOOD STANDING THEIR INVESTMENT POWERS ARE USED AND ANNUAL TAX RETURNS AND COMPANY REPORTS ARE FILED

DOUGLAS, SYMES AND BRISSENDEN

(In this connection, it should be mentioned that the Tenanbaum letter (Exhibit A-42) was not produced in the usual way in pre-trial proceedings. The respondent found it among some seized documents in another matter. The solicitors for the respondent showed it to the solicitors for the appellants. The appellants' solicitors showed it to Mr. Smith. Mr. Smith asked these solicitors—did they have to disclose it. The appellants' solicitors informed Mr. Smith that they did, and it was then disclosed.)

This so-called Tenanbaum letter and Mr. Smith's notes on his memorandum (Exhibit R-52) remove any suggestion of spontaneity or lack of specific solicitation that might otherwise be inferred from the contents of these said night letters.

Then, Mr. Cameron telephoned Mr. Smith at which time (predicated on a deal being subsequently made), the following were discussed or settled:

(a) that Price Waterhouse & Co. would resign as auditors after closing;

(b) there was a discussion as to the provisions of books of account other than the C. Smythe Limited minute book;

(c) there was a discussion as to how parties could arrive at final figures having regard to the four year reassessment limitation in the *Income Tax Act*;

(d) there was a discussion as to how soon Price Waterhouse & Co. had to ascertain the final figures for the transaction and it was decided that it would be settled at December 22, 1961.

The above is all recorded in the further notes made by Mr. Smith of his conversation (see Exhibit R-54).

On this same day (December 20, 1961), Mr. Peter Osler, Q.C., solicitor for Greenshields Inc. telephoned Mr. I. S. Johnston, Q.C., solicitor for C. Smythe Limited etc., saying he had been instructed to act in a transaction wherein the shares of C. Smythe Limited would be split, but Mr. Johnston told Mr. Osler that he lacked authority to proceed in

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this manner but would discuss the matter with his clients whereupon, Mr. Johnston, after consultation with Mr. Smith, advised Mr. Conn Smythe and Mr. C. Stafford Smythe that Mr. Smith thought the Greenshields Inc. scheme too devious, and at that time received instructions from them not to proceed with the proposed deal with Greenshields Inc. but rather to proceed with the Cameron transaction.

In other words, it was at this time a decision was made by the appellants *qua* shareholders in C. Smythe Limited not to proceed with a sale of the shares of C. Smythe Limited to a "dealer in securities" (Greenshields Inc.) but instead to proceed with a sale of such shares to the Cameron group at a price equivalent to a "dollar for dollar on capital and ninety-five per cent on undistributed income" (see Exhibit A-13); and the purported reason for the decision not to proceed with the proposed sale to this specific dealer in securities Greenshields Inc. was that their proposal was considered "too devious" and therefore might render the appellant shareholders liable for income tax because Greenshields Inc. required under its proposal that the shares of C. Smythe Limited be split before they would purchase them.

A fortiori, (it is hardly necessary to say) it was then decided that the transaction to be entered into with the Cameron group was not "too devious".

The matter of deviousness or not may perhaps be best adjudged by a more detailed narrative of what happened than would otherwise be made. There follows such a narrative.

That same day at about 11:30 a.m., Mr. Thom telephoned Mr. Smith and stated he had considered the matter requested by Mr. Smith the day before and discussed it with his partner, Mr. Wotherspoon; and that they both felt it would be quite in order for the shareholders to sell their shares to the Vancouver group and that Mr. Thom would recommend this course if it was his client. Mr. Smith then read the copies of the night letters, which he had received from Mr. Cameron and his solicitors, to Mr. Thom who said that Mr. Smith "had made inquiries beyond those which he would have considered necessary in the circumstances and that he would have no hesitation whatsoever in recommending the proposed sale". (See Exhibit A-41.)

(It perhaps should be noted in connection with Mr. Smith's telephone discussions with Mr. Thom, that what is significant is what was not told Mr. Thom of these proposed transactions and also what questions were not asked.)

On that same day, Mr. Smith discussed the transaction with Mr. Conn Smythe and told him he was checking the "bank credit" with the Bank of Montreal, Cameron's banker. It was at this time that Mr. Conn Smythe agreed that in computing the sale price of the shares there should be no adjustment to undistributed income more or less than a $5,000 variance from the original figures calculated. Mr. Conn Smythe also authorized Mr. Smith at that time to disclose the identity of C. Smythe Limited to Mr. Cameron. (See Mr. Smith's further notes, Exhibit R-55.)

Thereupon, Mr. Smith wired Mr. Cameron that the shareholders of C. Smythe Limited were interested in the night letter proposals, (see Exhibit A-19).

Then Mr. Cameron made an informal request of Mr. Peel, Bank of Montreal Manager, Hastings and Burrard Streets Branch, Vancouver, B.C., according to the evidence of Mr. Peel, for an accommodation for a short time to enable F. H. Cameron Limited and Dabne Enterprises Limited to purchase the shares of C. Smythe Limited.

Mr. Peel sought permission by way of telegram from the Bank of Montreal, Head Office Montreal, to make the temporary loan to F. H. Cameron Limited and Dabne Enterprises Limited for this purpose and obtained it (see Exhibits R-68 and A-20). (This loan was for $2,570,336.)

Mr. Smith telephoned Mr. Russell and requested him to check Mr. Cameron's bank credit. Mr. Smith at this time knew that it was only temporary financing that Mr.

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Cameron's group needed—that it was to be as it was put in the evidence—a "daylight loan". (In this connection, the evidence is that the Bank of Montreal knew the loan was for the purpose of what was colloquially called a so-called "dividend strip", and the bank charged a special fee for such a loan. The bank also knew they were going to be repaid this loan out of the cash assets of the company, C. Smythe Limited, the shares of which the Cameron group were purchasing and not from any assets of the Cameron group; and to be sure of this, the bank took the so-called "safety cheques" from the Cameron group as purported officers of C. Smythe Limited before these Cameron people had purchased the shares of that company, and did the other things hereinafter referred to.)

Mr. Russell then made inquiries of Mr. Peel as "to the ability of Cameron to carry through the transaction" with the assistance of the Bank of Montreal, Vancouver, B.C. Mr. Russell was informed by Mr. Peel that the assistance of the Bank of Montreal for this particular purpose would be forthcoming. (This assistance, as mentioned, was for a so-called "dividend strip".)

On the same day Mr. Cameron and Mr. Thompson attended Mr. Russell's office at Price Waterhouse & Co., Vancouver, and discussed arrangements for closing.

On December 21, 1961 Mr. Smith telephoned Mr. Cameron and they agreed that (a) closing would be either in Toronto or Vancouver, or in both cities at once, using conference telephones; and (b) a duplicate seal for C. Smythe Limited would be prepared and sent to Vancouver in order to pass the necessary banking by-law on the closing date.

On Friday December 22, 1961 Mr. Cameron had a telephone conversation with Mr. Smith and agreed (a) that prior to closing, the existing directors of C. Smythe Limited would resign and Cameron's nominees would be elected as directors "so that they could function" at closing; (b) that Mr. Russell would attend at closing in Vancouver and bring the duplicate seal of C. Smythe Limited;

(c) that the probable closing time would be December 28, 1961 at 1:30 p.m. Toronto time and (d) that at that time because final figures were still unknown Mr. Smith would call Mr. Cameron later and give him a "ceiling on gross amount". (See Exhibit R-59 and Exhibit R-88.)

Mr. Smith then telephoned Mr. Cameron that the ceiling on gross amount would be $2,650,000. (See Exhibit R-59.)

Mr. Smith then telephoned Mr. Conn Smythe and cleared the arrangements (See Exhibit R-59).

(On the following days, no action was taken for obvious reasons:

December 23, 1961—Saturday.

December 24, 1961—Sunday.

December 25, 1961—Christmas.

December 26, 1961—Boxing Day.)

On December 27, 1961 (Wednesday), Mr. Smith then prepared a memorandum of the proposal for "the use of two escrow agents". (See Exhibit R-62).

On this day also, C. Smythe Limited requested the International Division Branch of the Toronto-Dominion Bank to transfer title of the $800,000 fixed deposit to C. Smythe For Sand Limited for security to the bank in respect to the loan that was subsequently made by this bank to this latter company for the payment of this transaction.

Mr. Smith also telephoned Mr. Cameron and gave the final figures for closing, namely:

Total assets of old company (C. Smythe Limited)	$ 2,611,769
Undistributed income	$ 728,652
Discount of 5% of undistributed income	$ 36,433
Add all-round amount	5,000
	$ 41,433
Purchase price of shares	$ 2,570,336

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(In this connection, it should be noted that Mr. Cameron and his associate through F. H. Cameron Limited and Dabne Enterprises Limited were to (and did) receive this said sum of $41,433 for their part in implementing this transaction.)

Mr. Smith then prepared a balance sheet for C. Smythe Limited as at 12 noon E.S.T., December 28, 1961.

This balance sheet showed the sole asset of C. Smythe Limited to be $2,611,769. (See Exhibits R-61, A-28, A-29, A-30 and A-31.)

The plan to use escrow agents for closing was abandoned and arrangements were made with the Toronto-Dominion Bank for (a) the simultaneous exchange of its draft of $2,611,769 for the Bank of Montreal drafts totalling $2,570,336; and (b) for a temporary bank loan of $316,769 to cover the deficiency in the above drafts of $41,433 (this is the amount Mr. Cameron and his associates were to and did get) plus the amount of cash to be distributed to the shareholders of C. Smythe Limited, *viz.*, $275,336; and (c) to secure this temporary loan of $316,769 with the said fixed term deposit of $800,000, (this represented the sum obtained from the said sale by C. Smythe Limited of its shares in Maple Leaf Gardens Limited, which at the time were invested in U.S. (funds) and (d) for repayment of the temporary loan on January 2, 1962.

These arrangements were made pursuant to the recommendations of Price Waterhouse & Co. (S. E. V. Smith) to Mr. Conn Smythe (See Exhibit R-73).

Mr. Smith then prepared for the shareholders of C. Smythe Limited, a Pro Forma Balance Sheet as at December 15, 1961 after giving effect to the banking transactions on closing. This showed a bank overdraft of $316,769 and paid up capital of $10,000 and non-interest-bearing debentures $2,285,000 totalling in all $2,611,769. Attached to the Pro Forma Balance Sheet was a schedule showing the shareholders' ownership of these shares and debentures and the amounts of cash payable to each of them ($275,336). (See Exhibits A-32 and A-31.)

Then between December 28, 1961 and January 4, 1962, the following took place:

On December 28, 1961 (Thursday) the Bank of Montreal in Vancouver: (a) opened a bank account in the name of

C. Smythe Limited; and had prepared a draft banking resolution of C. Smythe Limited, appointing the Bank of Montreal as one of its banking agents and authorizing Mr. Cameron and Mr. Bone as signing officers; (b) drew "safety cheques" on the account of C. Smythe Limited and had them signed by Messrs. Cameron and Bone; and (c) issued instructions that the ledger card for C. Smythe Limited was to be kept separate and that no cheques were to be honoured on this account without the specific instruction from the manager who would then negotiate the safety cheques.

The Bank of Montreal also on December 28, 1961 obtained from F. H. Cameron Limited a promissory note for $1,285,000 and a promissory note from Dabne Enterprises Limited for $1,280,000.

Sums in these amounts were credited to the respective accounts of F. H. Cameron Limited and Dabne Enterprises Limited; and simultaneously there was drawn on these accounts, banker's drafts for $1,285,168 (Dabne) and $1,285,168 (Cameron) payable to the Toronto-Dominion Bank, Vancouver, which were held in escrow by Mr. Peel, the Bank of Montreal, Vancouver, Manager.

Then at 10.00 a.m. a directors' meeting of C. Smythe Limited was held wherein the by-laws were amended: (a) to permit shareholders meetings in Vancouver; and (b) to remove the chairman's casting vote.

Between 10:30 a.m. to 2:30 p.m., a shareholders' meeting of C. Smythe Limited was held wherein: (a) the sale of the assets was confirmed; (b) the resignations were accepted from Conn Smythe, C. Stafford Smythe, C. H. Day and A. M. Boyd as officers and directors; and (c) transfers of shares were made from Conn Smythe to F. H. Cameron, D. A. Bone, W. J. Thompson, W. G. Lane, W. H. Bouck, J. R. Hetherington, Ian Douglas and Ester Fortney.

At 2:30 EST, 11:30 PST, simultaneous meetings were held at: (a) Head Office, Toronto-Dominion Bank, Toronto; and (b) Main Branch, Toronto-Dominion Bank, Vancouver, at which the following transpired:

(i) the corporate seal and corporate records of C. Smythe Limited were handed over to the Cameron group;

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(ii) the banking resolution of C. Smythe Limited appointing the Bank of Montreal as its banking agent and authorizing Mr. Cameron and Mr. Bone as signing officers was executed by affixing the corporate seal of C. Smythe Limited;

(iii) shares of C. Smythe Limited were handed over to the Cameron group;

(iv) the bank drafts were exchanged between Bank of Montreal and Toronto-Dominion Bank.

The Toronto-Dominion draft of $2,611,769 was credited to the C. Smythe Limited account in Bank of Montreal, Vancouver.

The bank account of C. Smythe For Sand Limited was debited with a draft of $2,611,769 and credited with a draft for $2,295,000.

The Toronto-Dominion Bank, Toronto, then paid:

Conn Smythe	$ 143,175
C. Stafford Smythe	84,763
C. H. Day	44,054
A. M. Boyd	3,344
	$ 275,336

On January 2, 1962 (Tuesday), in Vancouver, at the Bank of Montreal, the following took place:

(a) Mr. Cameron and Mr. Bone each drew cheques for $1,305,600 against the Bank of Montreal account of C. Smythe Limited, and deposited them in the accounts of F. H. Cameron Limited and Dabne Enterprises Limited;

(b) simultaneously, the accounts of F. H. Cameron Limited and Dabne Enterprises Limited were debited to repay to the Bank of Montreal the temporary loans or accommodations of December 28, 1961; and

(c) the safety cheques drawn on the account of C. Smythe Limited were returned by Mr. Peel to Mr. Cameron and Mr. Bone, who destroyed them.

On the same day, at a director's meeting of C. Smythe Limited at 4:30 p.m., that company was authorized to and did invest $2,611,200 in preference shares of F. H.

Cameron Limited and Dabne Enterprises Limited (to put the latter two companies in funds to pay off the said loan to the Bank of Montreal).

In this latter connection, as the evidence clearly indicates, it is a proper inference to make and I do make it, that these preference shares of F. H. Cameron Limited and Dabne Enterprises Limited at the time of acquisition by C. Smythe Limited were valueless; and that as a consequence on that day, C. Smythe Limited (subsequently changed in name to C. S. Enterprises Limited) had no assets of any value, and its shares were worthless.

On January 4, 1962 Letters Patent for C. Smythe For Sand Limited were recorded.

It is also a reasonable inference to make and I do make it, that F. H. Cameron Limited and Dabne Enterprises Limited were engaged at the material time in schemes aimed at "stripping the surplus" of "old" companies which had converted its assets into cash by selling its operations and operating assets to "new" companies and that the appellants through their agent Mr. Smith had "actual knowledge" of this, and also that the surplus of C. Smythe Limited was going to be "stripped" by the purchaser of these shares without paying income tax. (c.f. Devlin J. in *Roper v. Taylor's Central Garages (Exeter), Limited*[7].)

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[7] [1951] 2 T.L.R. 284 at 288-89

. . .There are, I think, three degrees of knowledge which it may be relevant to consider in cases of this kind. The first is actual knowledge, which the justices may find because they infer it from the nature of the act done, for no man can prove the state of another man's mind; and they may find it even if the defendant gives evidence to the contrary. They may say, "We do not believe him; we think that that was his state of mind." They may feel that the evidence falls short of that, and if they do they have then to consider what might be described as knowledge of the second degree; whether the defendant was, as it has been called, shutting his eyes to an obvious means of knowledge. Various expressions have been used to describe that state of mind. I do not think it necessary to look further, certainly not in cases of this type, than the phrase which Lord Hewart, C.J., used in a case under this section, ***Evans v. Dell*** ((1937) 53 The Times L.R. 310), where he said (at p. 313): ". . .the respondent deliberately refrained from making inquiries the results of which he might not care to have."

The third kind of knowledge is what is generally known in the law as constructive knowledge: it is what is encompassed by the words "ought to have known" in the phrase "knew or ought to have known." It does not mean actual knowledge at all; it means that the defendant had in effect the means of knowledge. When, therefore, the case of

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Mr. Cameron apparently, through his company and others had engaged in about forty-five of these "dividend stripping" schemes.

(The scheme invoked here, to state it summarily, was for the "old" shareholders to withdraw their funds "tax free" by selling their "old" shares at a discount of 5 per cent of the undistributed earned surplus plus $5,000 or $41,433. The purchasers of these shares, F. H. Cameron Limited and Dabne Enterprises Limited, who purchased equal amounts of these shares, then recovered their money and their profit of $41,433 by issuing worthless preferred shares from F. H. Cameron Limited and Dabne Enterprises Limited to C. Smythe Limited in return for the cash.)

It may appear obvious that what was done in C. Smythe Limited by Mr. Cameron and associates was illegal having regard, among other things, to the provisions of the Ontario *Corporations Act*; but notwithstanding this does not affect the basis for this determination.

It may also appear obvious, that Mr. Russell, the "tax expert" of Price Waterhouse & Co. at Vancouver, B.C. did not know of any "magic" whereby the undistributed earned income of any company could be got out and distributed legally to the shareholders without paying income tax. Mr. Russell said so in evidence. And it is a reasonable inference and I make it, that Mr. Russell knew that Mr. Cameron, F. H. Cameron Limited or Dabne Enterprises Limited did not know of any such method either.

It is also a reasonable inference that Mr. Russell communicated his opinion to the said Mr. Smith, Toronto partner of Price Waterhouse & Co. who acted as agent for

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the prosecution is that the defendant fails to make what they think were reasonable inquiries it is, I think, incumbent on them to make it plain which of the two things they are saying. There is a vast distinction between a state of mind which consists of deliberately refraining from making inquiries, the result of which the person does not care to have, and a state of mind which is merely neglecting to make such inquiries as a reasonable and prudent person would make. If that distinction is kept well in mind I think that justices will have less difficulty than this case appears to show they have had in determining what is the true position. The case of shutting the eyes is actual knowledge in the eyes of the law; the case of merely neglecting to make inquiries is not knowledge at all—it comes within the legal conception of constructive knowledge, a conception which, generally speaking, has no place in the criminal law.

the appellants and C. Smythe Limited and did all the negotiations and did all the dealing to cause this transaction to be completed. If Mr. Russell did not express his views to Mr. Smith, then Mr. Smith, in any event, it is a proper inference and I make it, would know this from his own training and experience.

It follows from this that it is a reasonable inference and I make it, that Mr. Smith knew at the material time that Mr. Cameron and his associates were going to employ some device while avoiding paying income tax, to get the undistributed earned surplus out of C. Smythe Limited, even if Mr. Smith did not know and could not be expected to know that the device that would actually be employed was to cause C. Smythe Limited to invest in worthless preferred shares in F. H. Cameron Limited and Dabne Enterprises Limited.

The appellants had actual knowledge of all the matters Mr. Smith wrote and told them; and it follows also as a matter of law that all Mr. Smith's actual knowledge must be imputed to the appellants because Mr. Smith was their agent for all purposes of these transactions.

So much for the facts and explicit inferences made.

I now come to the issues for determination in these appeals and the determination of them.

The main issue for decision is whether or not these transactions resulted in the conferral of a benefit on the appellants within the meaning of subsection (2) of section 137[8] of the *Income Tax Act*; and in the event that the decision on the main issue is in the affirmative, a subsidiary

[8] 137. (2) Indirect payments or transfers. Where the result of one or more sales, exchanges, declarations of trust, or other transactions of any kind whatsoever is that a person confers a benefit on a taxpayer, that person shall be deemed to have made a payment to the taxpayer equal to the amount of the benefit conferred notwithstanding the form or legal effect of the transactions or that one or more other persons were also parties thereto; and, whether or not there was an intention to avoid or evade taxes under this Act, the payment shall, depending upon the circumstances, be

(*a*) included in computing the taxpayer's income for the purpose of Part I,

(*b*) deemed to be a payment to a non-resident person to which Part III applies, or

(*c*) deemed to be a disposition by way of gift to which Part IV applies.

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issue for decision is whether the amount of such benefit should be assessed under section 8(1)[9] or section 81(1) of the *Income Tax Act.*

In respect to the main issue reference was made by counsel to three other statutory enactments respecting the taxation of corporate distributions, two of them in other jurisdictions and the third in the *Income Tax Act* of Canada.

Enactments in the two other jurisdictions are section 260[10] of the Australian Act, and section 28[11] of the (UK) *Finance*

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[9] 8(1) Appropriation of property to shareholders—Stock dividends and stock rights. Where, in a taxation year,

(*a*) a payment has been made by a corporation to a shareholder otherwise than pursuant to a *bona fide* business transaction,

(*b*) funds or property of a corporation have been appropriated in any manner whatsoever to, or for the benefit of, a shareholder, or

(*c*) a benefit or advantage has been conferred on a shareholder by a corporation,

otherwise than

(i) on the reduction of capital, the redemption of shares or the winding-up, discontinuance or reorganization of its business,

(ii) by payment of a stock dividend, or

(iii) by conferring on all holders of common shares in the capital of the corporation a right to buy additional common shares therein,

the amount or value thereof shall be included in computing the income of the shareholder for the year.

[10] 1200 ss. 257-260
(1748)

260. Every contract, agreement, or arrangement made or entered into, orally or in writing, whether before or after the commencement of this Act, shall so far as it has or purports to have the purpose or effect of in any way, directly or indirectly—

(*a*) altering the incidence of any income tax;

(*b*) relieving any person from liability to pay any income tax or make any return;

(*c*) defeating, evading, or avoiding any duty or liability imposed on any person by this Act; or

(*d*) preventing the operation of this Act in any respect,

be absolutely void, as against the Commissioner, or in regard to any proceeding under this Act, but without prejudice to such validity as it may have in any other respect or for any other purpose.

[11] 28. Cancellation of tax advantages from certain transactions in securities.

(1) Where—

(*a*) in any such circumstances as are mentioned in the next following subsection, and

Act, 1960 as amended; the *Income Tax Act* of Canada, section 138A[12] (which was enacted in 1963).

In connection with these three enactments, the appellants say that section 260 of the Australian Act and section 28 of the (U.K.) *Finance Act 1960* as amended are equivalent legislation to section 138A of the *Income Tax Act* of Canada, while the respondent submits that section 260 of the Australian Act is more, in purpose and effect, like section

(*b*) in consequence of a transaction in securities or of the combined effect of two or more such transactions,

a person is in a position to obtain, or has obtained, a tax advantage, then unless he shows that the transaction or transactions were carried out either for bona fide commercial reasons or in the ordinary course of making or managing investments, and that none of them had as their main object, or one of their main objects, to enable tax advantages to be obtained, this section shall apply to him in respect of that transaction or those transactions:...

[12] 138A. Dividend Stripping—Associated Corporations.

(1) Dividend Stripping. Where a taxpayer has received an amount in a taxation year.

(*a*) as consideration for the sale or other disposition of any shares of a corporation or of any interest in such shares,

(*b*) in consequence of a corporation having

(i) redeemed or acquired any of its shares or reduced its capital stock, or

(ii) converted any of its shares into shares of another class or into an obligation of the corporation, or

(*c*) otherwise, as a payment that would, but for this section, be exempt income,

which amount was received by the taxpayer as part of a transaction effected or to be effected after June 13, 1963 or as part of a series of transactions each of which was or is to be effected after that day, one of the purposes of which, in the opinion of the Minister, was or is to effect a substantial reduction of, or disappearance of, the assets of a corporation in such a manner that the whole or any part of any tax that might otherwise have been or become payable under this Act in consequence of any distribution of income of a corporation has been or will be avoided, the amount so received by the taxpayer or such part thereof as may be specified by the Minister shall, if the Minister so directs,

(*d*) be included in computing the income of the taxpayer for that taxation year, and

(*e*) in the case of a taxpayer who is an individual, be deemed to have been received by him as a dividend described in paragraph (*a*) of subsection (1) of section 38.

(2) Associated corporations. Where, in the case of two or more corporations, the Minister is satisfied

(*a*) that the separate existence of those corporations in a taxation year is not solely for the purpose of carrying out the business of those corporations in the most effective manner, and

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137(2) of the *Income Tax Act* of Canada, but concedes that section 28 of the (U.K.) *Finance Act 1960* as amended is similar in purpose and effect to section 138A of the *Income Tax Act* of Canada.

Decisions under these said Australian and United Kingdom statutes are helpful in considering the judicial approach to the matter of the taxation of certain corporate distributions. (See *Newton v. Commissioner of Taxation*[13]; *Hancock v. Commissioner of Taxation*[14]; *Bell v. Federal Commissioner of Taxation*[15]; *I.R.C. v. Brebner*[16].)

But in coming to a conclusion in this case, however, it is necessary to refer specifically only to the provisions of sections 8(1), 81(1) and 137(2) of the *Income Tax Act,* and to consider their meaning and effect as applied to the facts of this case.

Before considering the applicability of section 137(2) of the *Income Tax Act,* it is necessary to consider firstly

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(*b*) that one of the main reasons for such separate existence in the year is to reduce the amount of taxes that would otherwise be payable under this Act

the two or more corporations shall, if the Minister so directs, be deemed to be associated with each other in the year.

(3) Appeal. On an appeal from an assessment made pursuant to a direction under this section, the Tax Appeal Board or the Exchequer Court may

(*a*) confirm the direction;

(*b*) vacate the direction if

(i) in the case of a direction under subsection (1), it determines that none of the purposes of the transaction or series of transactions referred to in subsection (1) was or is to effect a substantial reduction of, or disappearance of, the assets of a corporation in such a manner that the whole or any part of any tax that might otherwise have been or become payable under this Act in consequence of any distribution of income of a corporation has been or will be avoided; or

(ii) in the case of a direction under subsection (2), it determines that none of the main reasons for the separate existence of the two or more corporations is to reduce the amount of tax that would otherwise be payable under this Act; or

(*c*) vary the direction and refer the matter back to the Minister for reassessment.

[13] [1958] A.C. 450.
[14] (1962-63) 108 C.L.R. 259.
[15] (1952-53) 87 C.L.R. 548.
[16] [1967] 1 All E.R. 779.

section 137(3)[17] because that subsection puts a limit on the application of section 137(2), by prescribing that it does not apply to a transaction that was entered into by:

(a) persons dealing at arm's length,

(b) *bona fide,*

(c) not pursuant to, or as part of, any other transactions (and other matters not relevant here);

For all three reasons spelled out in it, I am of the opinion that this subsection is not applicable to this transaction, in that (1) this transaction was pusuant to and part of other transactions; (2) that this was not a *bona fide* transaction, not in the sense of being fraudulent but instead in the sense of being not for any legitimate business purpose, in that it was entered into solely as a means of avoiding the taxation consequences of complying with the provisions of section 105 or section 105B of the *Income Tax Act*; and (3) that one interrelated part of the whole transaction, namely, the transaction between C. Smythe Limited and C. Smythe For Sand Limited was not a transaction entered into by persons dealing at arm's length.

Section 137(2) of the *Income Tax Act* reads as follows:

> 137(2) Indirect payments or transfers. Where the result of one or more sales, exchanges, declarations of trust, or other transactions of any kind whatsoever is that a person confers a benefit on a taxpayer, that person shall be deemed to have made a payment to the taxpayer equal to the amount of the benefit conferred notwithstanding the form or legal effect of the transactions or that one or more other persons were also parties thereto; and, whether or not there was an intention to avoid or evade taxes under this Act, the payment shall, depending upon the circumstances, be
>
> (*a*) included in computing the taxpayer's income for the purpose of Part I,
>
> (*b*) deemed to be a payment to a non-resident person to which Part III applies, or
>
> (*c*) deemed to be a disposition by way of gift to which Part IV applies.

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[17] 137. (3) Arm's length. Where it is established that a sale, exchange or other transaction was entered into by persons dealing at arm's length, *bona fide* and not pursuant to, or as part of, any other transaction and not to effect payment, in whole or in part, of an existing or future obligation, no party thereto shall be regarded, for the purpose of this section, as having conferred a benefit on a party with whom he was so dealing.

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In the consideration of the applicability of section 137(2) of the *Income Tax Act* to the facts of these cases, two tests may be and are now employed, namely, (1) by using some of the accounting employed in this transaction, and (2) by putting and answering in words four questions.

To demonstrate, by using some of the accounting, what was done here in relation to the applicability of section 137(2) of the Act, may be accomplished by reference to the journal entries dated December 15 and 28, 1961 made in the books of C. Smythe For Sand Limited. They show beyond the possibility of doubt what the "result" was of what was done when there is added to them, amounts representing the said payment in cash of $275,336 to the appellants and A. M. Boyd and of $41,433 to Cameron and associates.

These journal entries made are as follows:

C SMYTHE FOR SAND LIMITED
JOURNAL ENTRIES

1961		Dr	Cr
Dec. 15	Subscriptions Receivable ....$	4 00	
	To Common Shares		$ 4.00
	To record the subscription and issue on December 15, 1961 of four common shares of a par value of $1 00 each to the four incorporators of the company		
	(Directors' minutes December 15, 1961)		
Dec. 15	Subscriber—Conn Smythe	1.00	
	C. Stafford Smythe	1.00	
	C. H. Day	1.00	
	A. M. Boyd	1 00	
	To Subscriptions Receivable		4.00
	To transfer subscriptions receivable		
Dec. 15	Subscriber—Conn Smythe	5,199.00	
	C. Stafford Smythe	3,079.00	
	C. H. Day	1,599.00	
	A. M. Boyd	119.00	
	To Common Shares		9,996 00
	To record the subscription and allotment on December 15, 1961 of 9,996 common shares of a par value of $1.00 each as follows:		
	Conn Smythe	5,199	
	C. Stafford Smythe	3,079	
	C. H. Day	1,509	
	A. M. Boyd	119	
	(Directors' minutes December 15, 1961)		

Dec. 28	Subscriber—Conn Smythe	1,188,200.00	
	C. Stafford Smythe	703,820.00	
	C. H. Day	365,600 00	
	A. M. Boyd	27,380.00	
	To Non-interest Bearing Debentures		2,285,000 00
	To record the allotment and issue of non-interest bearing debentures on December 28, 1961 (full payment received in cash on that date) as follows:		
	Conn Smythe	1,188,200.00	
	C. Stafford Smythe	703,820.00	
	C. H. Day	365,600.00	
	A. M. Boyd	27,380.00	
	(Directors' minutes December 28, 1961)		
Dec. 28	Due to C. Smythe Limited	$2,611,769.00	
	To Toronto-Dominion Bank, Queen and Ossington Branch, Toronto, General Account		$2,611,769.00
	To record bank draft drawn payable to C. Smythe, Limited in full settlement of the amount due to that company		
Dec. 28	Toronto-Dominion Bank, Queen and Ossington Branch, Toronto—General Account	2,295,000.00	
	To Subscriber—Conn Smythe		1,193,400.00
	C. Stafford Smythe		706,900.00
	C. H. Day		367,200.00
	A. M. Boyd		27,500.00
	To amount credited by the bank to C. Smythe For Sand Limited representing payments by the above named individuals to the company (see copy of letter attached)		

To say in words what was done here in relation to the applicability of section 137(2) of the *Income Tax Act,* may be accomplished by putting and answering four (4) questions, *viz*:

1. WHAT WAS THE "RESULT" OF THESE TRANSACTIONS?

The old company (C. Smythe Limited) had assets worth $2,611,769.

(a) before the sale of its assets to the new company (C. Smythe For Sand Limited)

and

(b) also after the sale to new company, *but* after all these transactions took place

(c) the old company was left with assets that were valueless, *viz.,* preferred shares in F. H. Cameron Limited and Dabne Enterprises Limited.

2. WHERE DID ASSETS OF OLD COMPANY GO?

The assets went:

(a) to the new company (which became owned by the shareholders of old company, by way of common shares and non-interest-bearing debentures);

(b) $275,336 in cash went to the appellant shareholders and A. M. Boyd; and

(c) $41,433 in cash went to Mr. Cameron and his associates as a fee.

3. WAS A "BENEFIT" CONFERRED ON THE SHAREHOLDERS OF THE OLD COMPANY BY THE DISPOSAL OF ITS ASSETS IN THIS FASHION?

The "benefit" conferred on the shareholders and A. M. Boyd of the old company was:

(a) $275,336 in cash;

(b) $453,316 of the total of non-interest-bearing debentures in the new company (which debentures had a real value because on the assets side of the balance sheet of the new company, C. Smythe For Sand Limited, were the working and other tangible and intangible assets formerly belonging to the old company).

(The amount of these debentures received as a part of the said "benefit" equals: the difference between $728,652 undistributed earned surplus of the old company, C. Smythe Limited, and the said $275,336 received in cash).

4. WHAT "PERSON" CONFERRED THE SAID "BENEFIT" ON THESE APPELLANT "TAXPAYERS", AND WERE THERE "ONE OR MORE PERSONS.... ALSO PARTIES THERETO"?

The "person" the old company (acting through its officers and directors, the appellants who were controlling shareholders of it) with the help of and as "parties thereto", the following namely, and others,

(a) F. H. Cameron Limited,

(b) Dabne Enterprises Limited,

(c) F. H. Cameron personally,

(d) The Bank of Montreal, Vancouver, B.C.,

(e) The Toronto-Dominion Bank at Toronto and Vancouver

conferred this said "benefit" (i.e. as set out in 3 above) on the appellant shareholders and A. M. Boyd.

To consider further the applicability of section 137(2) of the *Income Tax Act* to the facts of these cases, these facts may be summarized in the manner following, that is to say:

Immediately before the series of transactions, the situation was that the old company (C. Smythe Limited) had substantial assets and the appellants (and A. M. Boyd) owned all the shares in the old company.

The straightforward way for the old company to have conferred on the appellants (and A. M. Boyd) the benefit to which they were entitled *qua* shareholders was for the old company to pay each of them a dividend. (The re-assessments herein were made on the basis that the appellants were deemed to have received a dividend.) (Such a benefit of course would have been subject to resultant income tax liability.)

If such a benefit (dividend) had been conferred (paid), the "result" would have been that the appellants would then have had the dividend (cash and securities) and they would still have had the shares in the old company which would then have had its original assets less the dividend.

But instead of the above, as a result of the series of transactions implemented in 1961, the situation was that the appellants had a "benefit" (cash and certain non-interest-bearing debentures in a new company, (C. Smythe For Sand Limited) and the shares in the new company which had all the assets of the old company minus that "benefit" and also minus the expense of carrying out the series of transactions. This is the important fact; for the only money or property that entered into the series of transactions, other than that which originated in the old company, was the money borrowed temporarily from the banks which went back to the banks.

The "result" of the whole series of transactions was therefore the same as if the old company had paid a dividend to the appellants (and A. M. Boyd) except that instead of the appellants (and A. M. Boyd) then owning

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shares in the old company and the old company having all its original assets minus the dividend, the appellants then owned shares in the new company that had all the old company's original assets minus the "benefit" and minus also the cost of carrying out the transactions. (From the appellants' point of view this was an immaterial difference except for the fact that the assets now belonging to the new company were somewhat less than if a dividend had been paid directly to them from the old company.)

The "result" of the series of transactions was therefore that the old company conferred a "benefit" on the appellants *qua* shareholders equal to the amount (cash and non-interest-bearing certificates in the new company) that they so acquired. Before the series, assets representing that amount belonged to the old company. After the series, they belonged to the appellants (and A. M. Boyd). If the appellants (and A. M. Boyd) had not been shareholders in the old company before the series, they would never have received these assets.

From all this it follows, in my view, that "notwithstanding the form or legal effect of the transactions", the said "benefit", because of section 137(2) of the *Income Tax Act* is deemed to be a "payment" to these appellant taxpayers "equal to the amount of the benefit conferred" and as a consequence such "payment" must be "included in computing the taxpayer(s)' income for the purpose of Part I" of the *Income Tax Act.*

"For the purpose of Part I" the amount of this benefit in the circumstances of this case could be assessed pursuant to the provisions of either section 8(1) or section 81(1) of the *Income Tax Act.*

The decision as to whether such benefit should be assessed under either section 8(1) or section 81(1) depends on a conclusion as to whether or not what was done here constituted a "winding-up, discontinuance or re-organization" of the business of C. Smythe Limited as those words are employed respectively in section 8(1) and section 81(1) of the Act.

The assessor in making the re-assessments for each of the appellants concluded that there was a "winding-up, discontinuance or re-organization" of C. Smythe Limited by reason of what was done here. As a consequence, because

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section 81(2)[18] so prescribes, the benefit received by the appellants was "deemed to be a dividend" and the assessor in making such re-assessments allowed the appellants a dividend credit pursuant to the provisions of section 38(1)[19] of the *Income Tax Act*.

Without deciding, if I had been in the position of the assessor I think I would have come to the conclusion that there was no "winding-up, discontinuance or re-organization" of the business of C. Smythe Limited, by reason of what was done here, within the meaning of those words as employed in sections 8(1) and 81(1) of the Act; and as a consequence, I would have assessed the "benefit" as income received by the appellants within the purview of section 8(1) of the *Income Tax Act* and as a consequence there would have been no dividend credit allowed to the appellants.

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[18] 81. (2) Deemed to be dividend. Where a corporation, at a time when it had undistributed income on hand, has

(*a*) redeemed or acquired any of its common shares or reduced its common stock, or

(*b*) converted any of its common shares into shares other than common shares or into some obligation of the corporation,

a dividend shall be deemed to have been received at that time by each of the persons who held any of the shares at that time equal to the lesser of

(i) the amount received or the value of that which was received by him for or in respect of the shares on the reduction or conversion, or

(ii) his portion of the undistributed income then on hand.

[19] 38. (1) An individual who was resident in Canada at any time in a taxation year may deduct from the tax otherwise payable under this Part for a taxation year 20% of the amount by which

(*a*) the aggregate of all dividends received by him in the year from taxable corporations in respect of shares of the capital stock of the corporations from which they were received and of all dividends that he is, by subsection (3) of section 8 and section 81, deemed to have received from such corporation in the year, to the extent that the dividends so received or so deemed to have been received, as the case may be, were included in computing his income for the year,

exceeds the aggregate of

(*b*) the amount, if any, deductible from income in respect of those dividends by virtue of a regulation made under subsection (2) of section 11, and

(*c*) all outlays and expenses deductible in computing the taxpayer's income for the year to the extent that they may reasonably be regarded as having been made or incurred for the purpose of earning the dividend income.

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One other comment collaterally, perhaps should be made, namely, that an appeal from an assessment made under sections 8(1), 81(1) and 137(2) of the Act is processed in the usual manner which involves an adjudication by the Court upon the facts in relation to the provisions of these sections of the Act. Under section 138A, however, an appeal is from the "direction" of the Minister of National Revenue, where there has been included in income an amount by the exercise of a ministerial discretion, and on such appeal the Court in its adjudication is prescribed by the narrow limits of appeals from such a discretion.

One final comment, also, perhaps should be made, and that is the reference to use of the word "conspiracy" in the pleadings of the respondent in this case, and the connotation put on it by counsel for the appellants that such was tantamount to an allegation of fraud on the part of the appellants in this case. In my view, no such connotation can be inferred here. While not having the precise elements of "civil conspiracy", the wording of sections 8(1) and 81(1) and especially section 137(2) of the *Income Tax Act* (when it refers to a person conferring a benefit and the fact that there may be one or more persons as "parties thereto") permits in the pleadings the employment of the concept of civil conspiracy in cases such as this and at the trial the leading of evidence of all of the transactions in the whole series, as was done in these cases.

In the result, therefore, the re-assessments are confirmed, and the appeals are dismissed with costs.

BETWEEN:

BRITISH PACIFIC LIFE INSURANCE COMPANY .... APPELLANT;

Toronto 1968 Feb. 13-16 Feb. 23

AND

THE MINISTER OF NATIONAL REVENUE .... RESPONDENT.

Income—Income Tax Act, R.S.C. 1952, c. 148, s. 30,—"A life insurance corporation"—It is not the function of the Court to add words in interpreting the words of a statute.

The appellant was incorporated by Private Act of the Parliament of Canada to "make contracts of life insurance, personal accident insurance and sickness insurance".

In 1959, the appellant acquired the rights and property and assumed the obligations and liabilities of British Pacific Insurance Company, a provincial corporation which was engaged in the accident and health business only.

The appellant continued to carry on this business, and in addition it immediately engaged in the life insurance business.

In the taxation years 1959, 1960 and 1961, the life insurance part of the appellant's business was relatively small in relation to its total business.

The respondent re-assessed the appellant for income tax during these years in accordance with the provisions of the *Income Tax Act* other than section 30 on the basis that the appellant was not a life insurance company within the meaning of section 30 of the *Income Tax Act* because (1) it at no relevant time carried on the business of life insurance exclusively; or alternatively (2) during the said taxation years, the predominant business of the appellant was not life insurance.

Held, the appeal should be allowed with costs.

For the reasons stated in the judgment, the Court came to the conclusion that on a true interpretation of section 30 of the *Income Tax Act* in relation to the facts of this case, the appellant was "a life insurance corporation" within the meaning of those words in that section.

INCOME TAX APPEAL.

C. F. H. Carson, Q.C. and *S. D. Thom, Q.C.* for appellant.

C. R. O. Munro, Q.C. and *G. V. Anderson* for respondent.

GIBSON J. (orally):—This appeal is from the re-assessments for income tax dated March 22, 1965, for the taxation years 1959, 1960 and 1961 of the appellant.

The appellant was incorporated by Private Act of the Parliament of Canada assented to May 5, 1959, being 7-8

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Elizabeth II, chapter 58, with power to "make contracts of life insurance, personal accident insurance and sickness insurance". (See Exhibit A-1). The appellant is a wholly-owned subsidiary (except for some qualifying shares) of Beneficial Standard Life Insurance Company, whose head office is in California.

In 1959 the appellant acquired the rights and property and assumed the obligations and liabilities of British Pacific Insurance Company, a provincial corporation incorporated under the British Columbia *Companies Act*. This provincial company was engaged in accident and health insurance business; it did no life insurance business. All staff and the business assets of this provincial company were taken over by the appellant, and it continued to carry on the accident and health business, and in addition it immediately engaged in the life insurance business.

Beneficial Standard Life Insurance Company subscribed $500,000 of the capital stock of the appellant and paid it up. It also made a contribution of $500,000 to the surplus of the appellant before the appellant commenced business.

By Certificate of Registry under the *Canadian and British Insurance Companies Act* issued by the Department of Insurance, Canada[1], on September 3, 1959, the appellant was authorized to transact in Canada the business of life insurance, personal accident insurance and sickness insurance and from that day to date, the appellant engaged in such business (see Exhibit A-8). Such Certificate of Registry was maintained in good standing at all relevant times.

The combined ordinary and group life insurance business of the appellant in force increased from $956,809 at the end of 1959 to $12,486,603 at the end of 1967 (see Exhibit A-25).

Commencing in the year 1959 and continuing to the present time the appellant has been actively engaged in the business of life insurance and has laid out substantial amounts of money and effort in the promotion of such business (see Exhibit A-24).

At all relevant times the appellant also has been accepted as a life insurance company by the Department of Insurance of Canada.

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[1] 1952 Statutes of Canada, Chapter 31.

In the year 1959 and subsequent years certain amounts were credited or deemed to be credited to the shareholders' account of the appellant and taxes were paid thereon pursuant to the provisions of section 30 of the *Income Tax Act* as follows:

	1959	1960	1961
Credit to shareholders' account	$ 1,746.00	$ 22,179.00	$ 23,314.00
Tax paid	331.07	4,112.74	4,198 62

By Notices of Re-assessment dated March 22, 1965, the Minister of National Revenue added to the appellant's income certain amounts described as "Additional Income as reported by the Superintendent of Insurance" to the taxable income of the appellant for the years 1959, 1960 and 1961.

The amounts so added according to the Minister were "computed in accordance with the provisions of the *Income Tax Act* other than section 30 thereof" and were $25,385.50, $107,408.67 and $300,454.34 respectively.

The dispute between the parties as to the amount of income tax payable for the three years in question as a consequence is substantial, being of the order of $168,000.

According to the pleadings of the Minister, in making these re-assessments the Minister acted on the following assumptions:

(a) The Appellant was carrying on the business of transacting accident and sickness insurance as well as life insurance during the taxation years in question herein.

(b) The premiums received by the Appellant in respect of life insurance policies during the taxation years 1959, 1960 and 1961 comprised .16 per cent, 1.02 per cent and 1.68 per cent respectively of the total premiums received by the Appellant in respect of accident and sickness and life insurance policies during the said taxation years.

(c) The Appellant was not a life insurance corporation within the meaning of section 30 of the *Income Tax Act,* Revised Statutes of Canada 1952, Chapter 148, and its taxable income therefore was not to be computed in the manner prescribed by the said section.

In consequence of those assumptions the Minister pleaded in his reply as follows:

(a) The Respondent says that the Appellant was not a life insurance corporation within the meaning of section 30 of the *Income Tax Act* Revised Statutes of Canada 1952, Chapter 148, and its taxable income is not to be computed in the manner prescribed by the said section.

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(b) In the alternative if the Appellant is a "life insurance corporation" within the meaning of section 30 of the *Income Tax Act* Revised Statutes of Canada 1952, Chapter 148, the Respondent submits that the Appellant is entitled by virtue of the said section to compute in the manner prescribed therein its taxable income derived from its life insurance business only; and the taxable income derived from all other business of the Appellant is to be computed in accordance with the provisions of the *Income Tax Act* other than the said section 30.

The facts upon which the Minister relies for such reassessments are also put in written answers to the undertaking given by counsel for the respondent on the examination for discovery of H. A. Stevens, an official of the respondent, as follows: (see page 3 of Exhibit A-2)

The facts relied upon for the allegation that the Appellant is not a life insurance corporation are:

(a) it has at no time carried on the business of life insurance exclusively, or alternatively,

(b) during the taxation years in question the predominant business of the Appellant was not life insurance.

The facts relied upon at this time in relation to (b) are:

(1) the Appellant is merely the successor of the British Pacific Insurance Company which at no time sold life insurance, and

(2) during the taxation years in question

(i) the revenues of the Appellant were derived predominantly from its accident-health insurance business,

(ii) the majority of the Appellant's employees were engaged in its accident-health insurance business,

(iii) the volume of business done by the Appellant, in terms of numbers of policies written or placed was predominantly accident-health insurance,

(iv) the expenses incurred by the Appellant were predominantly in the course of its accident-health insurance business.

The then Minister of National Revenue, the late Honourable John R. Garland by letter dated March 11, 1964, to Mr. S. D. Thom, Q.C., put the issue in dispute in this way: (see page 29 of Exhibit A-3)

As agreed during our interview on February 21st I am writing you regarding the claim of your client, British Pacific Life Insurance Company, that it should be considered a life insurance corporation for the purpose of Section 30 of the *Income Tax Act*.

Further consideration has been given to the grounds on which the Department takes the position outlined in our letters of November 14th, 1963 and January 8th, 1964 and to the arguments advanced by Mr. Lando and yourself at our meeting. The opinion is still held that your client may not be treated in the manner it claims.

The difference of opinion in this matter which exists between Departmental officials and yourselves stems, of course, from differing interpretations of the term "life insurance corporation" in section 30.

You have indicated that in your opinion the mere possession of the power to transact life insurance business entitles a taxpayer to the benefit of section 30 even though it transacts other kinds of insurance business far greater in volume and importance than that of its life business. Some Departmental officials interpret the term to mean only corporations whose sole business is life insurance. In practice, such a restricted interpretation has not been adopted but it is insisted that a company's business be predominantly life insurance before it may be considered to be covered by the term for tax purposes. Your client's business consists almost entirely of the sickness and accident business taken over from its predecessor. It is understood that in 1962 life premiums made up less than 3% of total premiums. A company with such a small amount of life insurance business does not merit treatment as a life insurance corporation under the Department's interpretation of the term.

The discussions and correspondence we have had indicate that the views of Departmental officials on this matter are quite firmly held. It is felt therefore that assessment should be proceeded with and our Vancouver Office is being advised to this effect. There will be of course opportunity for further discussion at the appeal stage if you decide to take that course.

The appellant takes the position on this appeal that it never submitted, as stated in this letter, that "the mere possession of the power to transact life insurance business entitles a taxpayer to the benefit of section 30".

On November 17, 1964, the then Minister of National Revenue the Honourable E. J. Benson wrote a further letter to Mr. Thom, again setting out the issue in dispute and suggesting the manner in which it should be resolved. (See page 31 of Exhibit A-3).

I wish to acknowledge your letter of 31st August, 1964, with which you enclosed a memorandum dealing with the history of British Pacific Life Insurance Company and giving reasons why it is considered that the company should be regarded as a life insurance corporation under Section 30 of the *Income Tax Act*. I also acknowledge your letter of 15th September advising of the progress being made in the United States by Beneficial Standard Life Insurance Company, parent company of British Pacific.

Your submission and previous correspondence on this matter have been reviewed and I can well understand the difficulty that arises in interpreting Section 30 of the *Income Tax Act*. It seems clear that further discussions will not reconcile the conflicting views held by you and Departmental officials on the question of what constitutes a life insurance corporation under that section. The normal procedure in such circumstances is to let the Court decide the question of interpretation and in order to get the Court's opinion an assessment has to be made and an appeal must be lodged by the taxpayer.

I think that this case should now be permitted to follow this procedure. With this in mind I am giving instructions to the Taxation Division to proceed with the assessments on the basis previously proposed.

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In carrying out Mr. Benson's direction, on February 16, 1965, the Vancouver office of the Department of National Revenue wrote the appellant and therein asked it to elect to be assessed in either one of two ways. (See page 32 of Exhibit A-3). That letter reads in part as follows:

> If you wish the Life Department figures to be taxed under Section 30 of the *Income Tax Act,* the approximate taxes thereon would be:
>
> 1959 (re $ 1,746.00) .... $ 330.91
> 1960 (re $22,179 00) $4,112.81
> 1961 (re $23,314.00) $4,198.00
>
> At the same time the Casualty taxable amounts would be subject to tax at usual corporation rates by a separate calculation.
>
> As an alternative, if you prefer, and on the assumption you confirm the figures in the first paragraph, we are prepared to assess as follows:

	1959	1960	1961
Life	$ 1,372.00	($ 1,447.00) (Loss)	$ 18,150.00
Casualty	24,013.50	108,855.67	282,304.34
Taxable Amount	$25,385.50	$107,408.67	$300,454.34

> These taxable amounts would be taxed at the usual corporation rates set forth in Section 39 of the *Income Tax Act* and the rate as provided by the *Old Age Security Act.*
>
> Will you please consider the above and advise us which method you prefer. If you wish to have the two Departments netted we will expect you to continue on this basis.
>
> Your confirmation of the Life Department profits (loss) figures as set forth in our first paragraph, and your advice as to whether you wish the Life Department taxable incomes treated under Section 30 or that they be netted with the Casualty taxable amounts for the application of Section 39 rates is requested.
>
> Your reply within three weeks would be appreciated.

The appellant replied to this letter on February 26, 1965, as follows: (see page 36 of Exhibit A-3)

> Department of National Revenue (Ottawa) is well aware of the fact that, in our studied opinion, this Company comes squarely within the provisions of Section 30 of *Income Tax Act* and is not subject in any way, shape or form to the taxation you suggest. Under these circumstances it is our intention to appeal any such assessment, and we are advised that it would be improper for the Company at this time to make a selection of either of your alternate propositions.

The opinion of the Superintendent of the Department of Insurance of Canada was that the method that should be employed in taxing the income of the appellant during this relevant period is pursuant to the provisions of section

30 of the *Income Tax Act* and not pursuant to the provisions of the Act other than section 30, as was done by the said re-assessments for income tax.

At this trial, it was common ground between the parties that at all relevant times the appellant was engaged in a *bona fide* manner in the life insurance business.

At this trial, also, it was established in evidence that the predominant part of the business of the appellant during the years 1959, 1960 and 1961 was in the accident and health field and not in the life field, but that progressively this situation changed and by 1967, as noted, the amount of life insurance which the appellant had in force was very substantial, which result had come about by reason of the very considerable effort and expenditure of money by the appellant over the whole of the period since its incorporation and commencement of business in 1959 to 1967.

Counsel for the appellant submitted among other things that there was no definition of "a life insurance corporation" in section 30 or in any other section of the *Income Tax Act*; and that no regulation had been passed pursuant to the enabling authority of section 117(*b*) of the Act "prescribing the evidence required to establish facts relevant to assessments under this Act."; that the Minister to support these re-assessments was asking the Court to legislate by adding alternatively either the word "exclusive" or the word "predominantly" or equivalent words in section 30 of the *Income Tax Act* in relation to the business of "a life insurance corporation"; and that in any event the facts relied on by the Minister to support his submissions that "predominant" is the test to qualify the income of the appellant as eligible for taxation under section 30 of the Act as set out above, (see page 3 of Exhibit A-3) are not the critical facts, but instead (1) the matter of reserves, (2) the investment income and (3) the agency development expense, are more meaningful.

Counsel for the respondent submitted three alternative positions regarding the meaning of section 30 of the *Income Tax Act,* namely, (1) that "a life insurance corporation" is a corporation whose business is "exclusively" life insurance; or (2) that it is one whose business is "predominantly" life insurance; or (3) that section 30

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of the Act only applies *qua* the life insurance part of the business of a life insurance corporation that also carries on an accident and health business.

In support of these positions counsel among other things submitted: (1) that section 30 of the *Income Tax Act* is an exemption provision and if ambiguous, must be construed against the taxpayer; (2) that the equivalent of section 30 of the Act has been in the Canadian income statute since the first *Income Tax Act* in this country, *viz*, the *Income War Tax Act*, Statutes of Canada 1917, chapter 28; (3) that the meaning of a "life insurance corporation" must be used in the sense used by Parliament in 1917; and that in consequence it is proper to assume that when Parliament in this taxing statute (*The Income War Tax Act*) referred to a "life insurance corporation" it used the words in the same sense that it used them in legislation enacted for the purpose of regulating insurance corporations, and therefore *The Insurance Act*, Statutes of Canada 1917, chapter 29 is a statute in *pari materia*; that a proper inference to be drawn from the language employed in *The Insurance Act* of 1917, particularly section 8(1), section 31(1) and (6), section 79 and especially section 104 which purports to describe what is meant by "shareholders' account", is that Parliament only intended to grant a special right regarding the taxation of income *qua* the income from the life business only and not *qua* the income from the accident and health businesses; and that in fact Parliament intended that life insurance corporations should transact life business only; (4) that if section 30 of the *Income Tax Act* is not a continuation of the law of 1917, then Parliament intended that the business of a life insurance corporation be predominantly in the life field before such a corporation was entitled to be taxed under section 30 of the *Income Tax Act*, and that the omission of the word "predominant" or an equivalent word or words in section 30 of the Act to spell this out more unequivocally was because it was considered unnecessary in view of the said history of the enactment of this provision originally in the 1917 statute; and finally (5) that in employing section 30 of the *Income Tax Act* in taxing the income of a life insurance corporation, only the income of such corporation in so far as it is a life insurance corporation, is entitled to the benefit of this section, because again of the historical origin of this section when no one thought that a life insurance corporation would carry on any other business along with its life insurance business.

So much for the submission of counsel.

My reasons for coming to the conclusion that I do, may be put briefly: (1) the appellant is and was at all material times in the life insurance business in a *bona fide* manner and has expended most substantial effort and money from incorporation to date in getting into the life insurance business; (2) the 1948 *Income Tax Act* was an entirely new act, and the date of its enactment is the date which should be looked at in considering the meaning of "a life insurance corporation" in section 30 of the present Act; (3) section 30 of the *Income Tax Act* is not an exempting provision. It is a special provision prescribing the method to be employed in taxing the income of life insurance corporations, and is no different than, for example, section 69 of the Act which prescribes special provisions for the taxation of the income of investment companies; (4) the Act incorporating the appellant company at clause 6, authorized the appellant to be in the life insurance business; and the name granted in this Act by Parliament to the appellant, namely, British Pacific Life Insurance Company is some evidence of Parliament's intent; (5) the Certificate of Registry under the *Canadian and British Insurance Companies Act,* Statutes of Canada 1952, chapter 31, authorized the appellant to engage in the life insurance business; and Part IV of that Act applies to this appellant; (6) section 30 of the *Income Tax Act* is not an escape from taxation but merely a type of deferral[2]; (7) neither in section 30 nor in any other section of the *Income Tax Act* is there a definition of "a life insurance corporation"; (8) no regulations have been passed pursuant to the enabling provisions of section 117(*b*) of the Act "prescribing the evidence required to establish facts relevant to assessments under this Act" and the facts alleged and proved therefore are no guide as to what should be considered in coming to a conclusion as to what are the necessary constituent elements of a business of a corporation to qualify it as a "life insurance corporation" within the meaning of section 30 of the Act; (9) if

[2] (See in this connection section 84 of the *Canadian and British Insurance Companies Act.*)

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Parliament had meant to qualify section 30 of the Act with either the word "sole" or "exclusive" or the word "predominant" or with equivalent words in relation to the business of a "life insurance corporation", or to have it apply only to the life insurance part of the whole business of such a corporation as the appellant, it would have said so, as it did, for example, in section 13, section 83A(2), section 83A(3), section 83A(3a), section 83A(3b) and section 83A(3c) of the *Income Tax Act*; and finally (10) it is not the function of the Court to add words in interpreting the words of a statute. In this connection, the words of Lord Simonds in *Magor and St. Mellons Rural District Council v. Newport Corporation*[3] in relation to what was suggested as the correct procedure for a Court to adopt in interpreting a statute, namely, "What the legislature has not written, the court must write", are apposite here, namely:

> It appears to me to be a naked usurpation of the legislative function under the thin disguise of interpretation. And it is the less justifiable when it is guesswork with what material the legislature would, if it had discovered the gap, have filled it in. If a gap is disclosed, the remedy lies in an amending Act.[4]

For these said reasons, the conclusion that I have come to, is that on a true interpretation of section 30 of the *Income Tax Act* in relation to the facts of this case, the appellant is "a life insurance corporation" within the meaning of those words in that section.

It follows therefore that what is the subject matter of this appeal is the taxable income of the appellant from all sources and not just its income from one source, namely, the income from the life insurance part of its business; and the correct method of computing such taxable income is pursuant to section 30 of the *Income Tax Act* and not pursuant to the provisions of the Act other than section 30.

The appeal is therefore allowed and the re-assessments are vacated.

The appellant is entitled to its costs.

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[3] [1952] A.C. 189 at 191.

[4] Compare also Craies on *Statute Law, 6th Edition,* pages 70 and 71; and *3 Halsbury, Volume 36,* page 387.

BETWEEN:

HER MAJESTY THE QUEEN,

AND

J. W. MILLS & SON LIMITED, KUEHNE & NAGEL (CANADA) LIMITED, OVERLAND IMPORT AGENCIES LIMITED, DENNING FREIGHT FORWARDERS LIMITED, JOHNSTON TERMINALS LIMITED.

Vancouver 1967

Nov. 6-10, 13, 15-17, 20-24

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April 1

Combines—Conspiracy in the import pool business to carry into effect an anticompetitive trade practice or policy in a relevant competitive market—Element of "undueness" relating to limiting "the facilities for transporting or dealing" in articles or commodities subject of trade or commerce—Combines Investigation Act, R.S.C. 1952, c. 314, ss. 32(1)(a) and 32(1)(c).

The indictment found against the accused contained two counts alleging offences contrary to ss. 32(1)(*a*) and 32(1)(*c*) respectively of the *Combines Investigation Act* during the period between January 1st 1956 and August 1st 1966.

The accused were in the import pool business which concerned "articles" or "commodities" that may be the subject of trade and commerce imported from certain designated areas in the Orient which were transported by ship from such areas in the Orient to Vancouver, B.C., and which were then transported by railway in a certain category of railway car sometimes called Pool cars to points in Canada, east of Manitoba, Ontario boundaries, such points being mainly Toronto and Montreal, in which cities the importers of such articles or commodities had their places of business.

The two broad issues for adjudication were whether the indictment and the particulars thereof alleged and the evidence adduced proved beyond a reasonable doubt, an agreement to carry into effect an anticompetitive trade practice or policy in (1) a relevant competitive market; and (2) having the element of "undueness" relating to (*a*) (under count 1) limiting "the facilities for transporting or dealing" in articles or commodities that may be subject of trade or commerce (s. 32(1)(*a*)) of the *Act* and (*b*) (under count 2) preventing or lessening "competition in the transportation" of articles or commodities that may be subject of trade or commerce (s. 32(1)(*c*)) of the Act.

Held: (1) that the indictment and particulars alleged the true relevant market; and that the evidence proved such was the true relevant market in which these accused carried on their respective business at the relevant times, beyond a reasonable doubt.

(2) that the evidence also proved beyond a reasonable doubt that the behaviour or conduct of the accused (other than Denning Forwarders Ltd. and Johnston Terminals Limited) in such relevant market, employing the devices they did, had the necessary criminal elements of "undueness" so as to constitute the offences charged under both s. 32(1)(*a*) and s. 32(1)(*c*) of the *Combines Investigation Act.*

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(3) that the verdict of the court was therefore that the accused Overland Import Agencies Ltd., J. W. Mills & Son Limited and Kuehne and Nagel (Canada) Limited were guilty on both count 1 and count 2 of the indictment.

PROSECUTION under *Combines Investigation Act.*

R. P. Anderson, I. M. Wolfe and *D.W. Patterson* for the Queen.

R. M. Hayman for J. W. Mills & Son, Limited and Kuehne & Nagel (Canada) Limited.

J. G. Alley and *W. Hohmann* for Overland Import Agencies Limited.

Brenton D. Kenny and *Martin Gross* for Denning Freight Forwarders Limited.

G. S. Cumming and *D. T. Hopkins* for Johnston Terminals Limited.

GIBSON J.:—The indictment found against the accused contains two counts alleging offences contrary to sections 32(1)(*a*)[1] and 32(1)(*c*)[2] respectively of the *Combines Investigation Act.*

These sections make it an offence, among others, for any person to conspire, combine, agree, or arrange with another person (1) "to limit unduly the facilities for transporting ... or dealing in any article" or (2) "to prevent or lessen unduly competition in the ... transportation ... of an article ...".

The period prescribed in each count is between January 1, 1956 and August 1, 1966, both inclusive.

Particulars of this Indictment were given.

This Indictment and the Particulars are set out in full in Schedule "A" to these reasons.

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[1] 32. (1) Every one who conspires, combines, agrees or arranges with another person

(*a*) to limit unduly the facilities for transporting, producing, manufacturing, supplying, storing or dealing in any article,

. . .

[2] (*c*) to prevent, or lessen, unduly, competition in the production, manufacture, purchase, barter, sale, storage, rental, transportation or supply of an article, or in the price of insurance upon persons or property, or

. . .

All accused (who are sometimes called freight forwarders) at some or in some cases at all of the material times prescribed in the Indictment were in what is sometimes known as the import pool car business. Such business concerned articles or commodities that may be the subject of trade and commerce imported from certain designated areas in the Orient which were transported by ship from these areas in the Orient to Vancouver in the Province of British Columbia and which were then transported by railway in a certain category of railway car sometimes called pool cars to points in Canada east of the Manitoba-Ontario boundary, such points being mainly Toronto and Montreal in which cities the importers of such articles or commodities had their places of business.

The accused, Overland Import Agencies Ltd., at the time of the trial carried on business under the trade name of "Leimar Forwarding Co." (herein sometimes called "Leimar"). Originally when this business was established in July 1955, it was the pool car department of Leith & Dyke Limited, which latter company was a large customs brokerage firm in Vancouver. Subsequent to that, the business was carried on by Leithdyke Forwarders Limited; then under the name of Leimar Forwarding Co. which was a partnership of two entities namely, Leith Services Ltd. and Mardock Enterprises Ltd.; and then this partnership was dissolved and Mardock Enterprises Ltd. changed its name to Overland Import Agencies Ltd.; and then, as stated, this business was carried on under the trade name of Leimar Forwarding Co. and was solely owned by Overland Import Agencies Ltd.

The accused J. W. Mills & Son Limited (herein sometimes called "Mills") entered this business after the accused Leimar; and originally it obtained customers by cutting rates which Leimar countered with a rate war which lasted between the two companies for about six months. This was in 1958. This rate war then ceased, brought about by an agreement between Mills and Leimar dated October 3, 1958, which agreement was subsequently modified by a subsidiary agreement executed on October 7, 1958.

Mills is and was at all material times, a Canadian owned company of Kuehne & Nagel of Hamburg, which latter

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company also incorporated and owned another Canadian company namely, the accused Kuehne & Nagel (Canada) Limited. The latter and Mills were inter-related companies and acted in concert during the material period.

The accused, Denning Freight Forwarders Ltd. (herein sometimes called "Denning") became established in this business early in 1960. It was established by a Victor Denning who was then employed as Traffic Manager in Montreal by J. W. Mills & Son Limited. Denning very quickly cut into the business of Leimar and Mills and to such an extent that the latter two companies by agreement instituted a rate war in April 1960 against Denning which lasted until October 1960, by which time Denning, because of the damages done to it by this rate war, was advised to, and had instituted a civil action in the Supreme Court of Ontario for such damages for conspiracy against Mills and Leimar. In October 1960, this rate war came to an end when Mills and Leimar settled this civil conspiracy action with Denning and entered into an agreement by which among other things, they agreed to pay Denning a certain commission for five years, and to give Denning a certain right of renewal of this agreement, which will be discussed more fully in these reasons.

The accused, Johnston Terminals Limited (herein sometimes called "Johnston"), (which is and was at all material times, a very substantial Vancouver transport company) entered into the Oriental import pool car business in September 1960 and has continued in it up to the time of this trial.

In addition, there was one other company that entered into this business which is not an accused person. This company is known as Freight Consolidators of Canada Limited, a company owned by certain customs brokers in Toronto. It got into this business about 1963, but by August 1, 1966, which is the terminal period of the time prescribed in the Indictment, it had been most unsuccessful in obtaining any significant part of the business in this industry and market and was supported by only three or four importers of any size.

All accused pleaded not guilty.

Two collateral matters arose during the course of this trial.

Firstly, after plea, counsel for the accused moved to quash the Indictment on the grounds that it disclosed no offence.

Secondly, after all the evidence was adduced at the trial, Crown counsel applied for an amendment to the Indictment, namely, for the addition to each count of the words "which could be" after the words "Province of British Columbia and" and before the words "transported by railway in railway cars".

As to the first motion, the submission of counsel for the accused was that: the activities of the accused were not within the purview of section 32(1)(*a*) of the *Combines Investigation Act* as alleged in Count 1 in that the accused provided "services" only and not "facilities"; and that what the accused did was also not within the purview of section 32(1)(*c*) of the Act as alleged in Count 2 because the accused were not in the business of "transportation". In support of this, it was argued that the accused did not own the means or facilities of transportation, did not themselves provide transportation, that they did not have physical possession of the goods, that they did not have the responsibility for the safety of the goods, but instead that was the responsibility of the carrier, and that the service fee charged for what they did was for pure services.

The decision on these motions was adjourned until now.

As to this first motion, I am of opinion, firstly that the accused at all material times were in a business which is in a service industry which touched and concerned tangible things that is "articles" "that may be the subject of trade or commerce" and were not in a business in a service industry which related solely to the provision of services; and that there are no words in this subsection or in the Act generally and nothing in the jurisprudence in respect thereto which make the ownership of "facilities for transporting" articles or commodities that may be the subject of trade or commerce a necessary element to constitute an offence contrary to section 32(1)(*a*) of the *Combines Investigation Act*; and secondly, in respect to Count 2 alleging an offence contrary to section 32(1)(*c*) of the Act, for similar reasons as set out above, it is not necessary that the accused own the physical means of

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transportation to be in the transportation business so as to be capable of committing an offence contrary to that subsection.

Accordingly, this motion is dismissed.

As to the second motion to amend the Indictment, I am of opinion that as there is no prejudice to the accused, the application for the amendment to each of the counts should be and accordingly is granted. (These amendments are included and underlined in the copy of the Indictment set out in Schedule "A" hereto).

Aside from the general defence of the plea of not guilty, the defence of these accused (aside from the certain additional specific defences of the accused Denning and Johnston) was that the Crown has not alleged in the Indictment and Particulars, nor proved in evidence, beyond a reasonable doubt, a relevant market in which the conduct or behaviour of the accused had the necessary element of "undueness" contrary to these said subsections of the *Combines Investigation Act*.

The two broad issues for adjudication, therefore, are whether the Indictment and the Particulars thereof alleges, and the evidence adduced has proved beyond a reasonable doubt, an agreement to carry into effect an anti-competitive trade practice or policy in (1) a relevant competitive market; and (2) having the element of "undueness" relating to (*a*) (under Count 1) limiting "the facilities for transporting or dealing" in articles or commodities that may be the subject of trade or commerce (section 32 (1)(*a*) of the Act), and (*b*) (under Count 2) preventing or lessening "competition in the transportation" of articles or commodities that may be the subject of trade or commerce (section 32(1)(*c*) of the Act).

In general outline, the factual situation during the material time namely between January 1, 1956 and August 1, 1966 was as follows:

Firstly, the subject articles or commodities which were the subject of trade and commerce are those set out in Canadian Freight Association East Bound Import Freight Tariffs and in the supplements and amendments thereto being:

(a) Canadian Freight Association Tariff 70A; effective July 11, 1951;

(b) Canadian Freight Association Tariff 70B; effective June 23, 1961; and

(c) Canadian Freight Association Tariff 70C; effective May 29, 1963.

Tariff 70B replaced Tariff 70A and Tariff 70C replaced Tariff 70B.

The said articles and commodities prescribed in these Tariffs by the terms of it were articles and commodities imported from certain designated areas in the Orient—in the main from Japan, Taiwan and Hong Kong.

These Tariffs stipulated, among other things, the unit price for minimum mixed carload weights of these specified articles or commodities, at which designated carriers, including the Canadian Pacific Railways and the Canadian National Railways, might carry them.

In the importation process, these said articles or commodities were transported firstly by vessel to the Port of Vancouver in the Province of British Columbia, and then, at the rates prescribed in these Tariffs, were transported by rail carriers from Vancouver to destination points in Canada in the Provinces of Ontario and Quebec, such points being east of the Saskatchewan-Manitoba boundary and which points were mainly Toronto and Montreal.

These said Tariffs were approved by the Board of Transport Commissioners of Canada and had the force of law.

The Canadian Freight Association was and is an association consisting, among others, of all railways with termini in Canada.

Secondly, the volume of articles and commodities imported from the Orient and transported by rail, pursuant to the said Canadian Freight Association Tariffs 70A and 70C, as admitted by the Crown, "constitute only a small portion of the imports to Canada as a whole of the nature described therein from the area designated (in the Orient) in Tariffs 70A, 70B and 70C".

Thirdly, the critical feature of these Tariffs which gave rise to the accused being in the business they were, and conducting it in the way they did, out of which these charges arose, was the privilege of mixing a railway car—called the mixing privilege.

A few words of explanation of this will suffice.

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Generally speaking, a railway car consists of 30,000 pounds of freight.

In the trade the rates for all individual shipments are known as "L.C.L." or "less than carload lots" while carload shipments are known simply as carload lots "C.L.".

When two or more commodities are consolidated for shipment in a single railway pool car, the pool car is known as a "mixed car". The consolidation of shipments of approximately 30,000 pounds per railway car is made of individual shipments of importers who, as stated, were located mainly in Toronto and Montreal, and such shipments consist of articles or commodities of merchandise which they have imported from the said designated area in the Orient.

The mixed carload rates under these tariffs was much less than the "L.C.L." or "C.L." rates. For example, the mixed car rate at one juncture for a certain type of shipment was just a little more than one half of the "L.C.L." rate.

This "mixing" privilege was first granted by the publication by the Canadian Freight Association of an amendment in 1955 to their Tariff 70A. Until that time, no mixing privileges were permitted.

The purpose of this mixed carload rate of this Tariff was to provide competitive freight rates to consignees in eastern Canada so that these commodities or articles imported from the Orient would move by rail from Vancouver to eastern Canada, instead of by other transportation facilities, and at a total transportation cost competitive with the ocean rates by ship when such articles or commodities were imported and shipped from the Orient directly to New York and then trucked to eastern Canada or transported by ship to New Orleans and trucked to eastern Canada or transported by ship to Halifax or Montreal, and (since the opening of the Seaway) to Toronto.

The Railways were willing in 1955 to establish this mixed carload rate because they were losing this business to the ships. The purported reason they established this rate and made it especially applicable to eastern Canada mainly from Vancouver to Toronto and Montreal was so that they would not have to reduce their rates for all other traffic between intermediate points and thereby they could and were able to leave undisturbed their other "L.C.L." and "C.L." rates.

In addition, by their Rule 43[3], the Railways denied to themselves the privilege of consolidating into a mixed pool car the merchandise or commodities imported by more than one consignee; so that in the result all this business was available only to parties other than the Railways.

This business is that in which the accused became involved and engaged in at all material times.

Fourthly, these accused freight forwarders, in the carrying on of this business, obtained what was the equivalent of a power of attorney from individual importers in Toronto and Montreal and so became the one consignee of the merchandise and commodities of a number of importers; and thereby were able to obtain the benefit of these mixed carload rates pursuant to Tariffs 70A, 70B and 70C by consolidating into shipments of 30,000 pounds per railway car such individual shipments of such importers.

Fifthly, these said railway Tariffs when combined with a certain category of shipping rates known as "O.C.P. ocean rates" (Overland Common Point) (more fully described later), permitted Canadian railway carriers in Vancouver to offer such consignees in eastern Canada lower freight rates for articles and commodities imported to Canada from the said designated areas in the Orient and destined for these consignees in eastern Canada.

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[3] Rule 43

Section 1. Carriers' Agents must not act as Agents of shippers or consignees for the assembling or distribution of CL or LCL freight.

Section 2. Carriers' Agents at points of shipment must not accept freight to be carried at CL ratings or rates for distribution to two or more parties by Carriers' Agents at points of destination.

Section 3. (a) Carriers' Agents at points of destination must deliver freight carried at CL ratings to one consignee only, and must not accept orders from shippers or consignees calling for split deliveries according to brands, marks, sizes or other identification of packages.

(b) If at the request of the owner of the property or his authorized agent, a CL shipment is delivered to more than one consignee, LCL ratings or rates will be applied on the entire shipment, except that the portion delivered to any one consignee will be subject to Rule 15, Section 1.

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Speaking generally, the ocean freight rates for most ships arriving in Vancouver from the Orient are governed by a particular conference[4] known as the Trans-Pacific Freight Conference of Japan.

This Conference established basically two rates, namely, one rate for shipments to eastern Canada and the other rate for other shipments. The eastern Canada rates (technically known as "Overland Common Point (O.C.P.) rates") were lower than the other rates, and applied to imported articles or commodities destined for inland points in Canada east of the Saskatchewan-Manitoba boundary where carriage was made by rail. This eastern Canada rate was about 10 per cent less than the other rates which applied to articles or commodities destined for Vancouver only, or, for transportation by non-rail facilities destined for Vancouver or for points west of the Saskatchewan-Manitoba border, or for transportation by non-rail facilities to inland points in Canada.

The combination of the two rates therefore, that is, the O.C.P. rates and the rates under Tariffs 70A, 70B and 70C, the ocean and the rail rates, during the material times and at the present time were and are significant to any importer in eastern Canada, because they did and still do provide him with a dollar and cents basis for electing to choose one mode of transportation over another in respect to articles or commodities imported by him from the said designated areas in the Orient to his place of business in Canada. In the cases where a dollar and cents basis outweighed all other basis for decision, an election in favour of the mode of transportation permitting such an importer to take advantage of the combination of these two rates followed.

Such an importer had at all material times (and still has) a meaningful choice therefore of taking advantage of these two rates and causing his importation of articles or commodities from the said designated areas in the Orient to be shipped to Vancouver and then to him in Toronto or Montreal by rail in mixed pool cars, or of causing his importation to be delivered to him by ship to New York

[4] "Shipping conferences" are groups of formally linked steamship lines. See for a reference. Restrictive Trade Practices Commission 1965 on *"Shipping Conference Arrangements and Practices"*.

and by truck to Toronto or Montreal, or delivered to him by ship to Halifax and by truck to Montreal or Toronto, or delivered by ship to him directly to Montreal (and since the opening of the St. Lawrence Seaway) to Toronto.

Such a consignee also had the option of using air transport either directly from the Orient or from Vancouver.

In addition, there is and was also one further inducement for such an importer to elect or take advantage of the combination of the ocean and rail preferential rates established (the O.C.P. rates and the rates of Tariffs 70A, 70B and 70C), in preference to the rates by other transportations above noted, because the ocean and rail carriers as a further inducement to cause such eastern Canadian importers to elect so as to benefit them, also absorbed all the shipping and loading charges, all of the wharfage charges, and all of the rail carloading charges that would normally be assessed by steamship companies, the docks, and the railways respectively. The division of absorption of these charges is and was as follows:

> vessel unloading—payment 100% by vessel wharfage —payment 50% by vessel and 50% by railways; rail carloading—payment 100% by rail.

Sixthly, a freight forwarder, such as the accused, did the following jobs for any importer who requested services of it, that is to say:

(a) it assembled and consolidated or provided for the assembly and consolidating of shipments of articles or commodities imported from the said designated areas in the Orient and for the distribution of such consolidated shipments;

(b) it assumed the responsibility for the transportation of such articles and commodities from the point of receipt to the point of destination; and

(c) it utilized for the whole or part of the transportation of such shipments the services of a common carrier.

(It is of significance that a most important feature of this service was and is the provision of assembling and consolidating imported articles and commodities into railway carloads or truckload lots of numerous small shipments of imported articles and commodities of individual impor-

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ters, most of whom would not be importing sufficient articles or merchandise to make up a carload or truckload lot.

Another essential feature of a freight forwarder's business is also of significance and that is that, although he is not the beneficial owner of the goods, nevertheless, as the "named consignee" he assumes the responsibility for such goods from the time such goods are received from the consignor until they are delivered to the beneficial owner.)

Seventhly, when the accused entered this business in this service industry, and how in certain respects they carried on their respective businesses, was as follows:

As stated, until early in 1958, Leimar Forwarding Co. (and predecessor entities) were the sole mixed pool car freight forwarders in the business. At that time J. W. Mills & Son Limited and Kuehne & Nagel (Canada) Limited got into the business.

J. W. Mills & Son Limited entered this business obtaining customers by cutting rates and Leimar countered and got into a rate war with it, which rate war between these two companies lasted for about six months.

At that time, these two companies entered into an agreement to cease the rate war and to stabilize rates. This Agreement was dated October 3, 1958; and this Agreement was subsequently modified by a subsidiary Agreement executed on October 7, 1958.

The October 3, 1958 Agreement, among other things, specified that for a period of four months a differential was to be maintained between the rates of these two companies, that the rates of Mills were to be lower than those of Leimar by 3¢ per one hundred weight for quantities of 10,000 pounds or less; and the Agreement also provided that this differential progressively was to be reduced for higher volume shipments until the rates of both companies became identical on shipments of 20,000 pounds or more. This Agreement further provided that the rates were to remain in effect until February 14, 1959, at which time they were to be reviewed and revised. Also, a group of selected customers of each company were granted an exception from the rates and the terms agreed upon, and those selected customers were to continue receiving special rates.

In addition to this formal agreement on rates, these two companies also agreed that for a period of one month from the date of their Agreement they would neither solicit nor accept business from each other's customers.

The provisions of these 1958 Agreements were carried into effect by Mills and Leimar and rate schedules conforming to the provisions of such Agreements were issued by both companies.

Thereafter there were various changes in some of the rates, sometimes arising in part from changes in railway tariffs on which they were based, which changes were also agreed to after discussion and consultation between Mills and Leimar.

These October 1958 Agreements provided for their renewal in February 1959; and in implementation of such provision on February 27, 1959, a new Agreement was entered into by these companies amending and expanding the October 1958 Agreements and removing the rate differential by reducing the Leimar rates to the same level as those of Mills. Subsequently, namely, from the day of these Agreements until August 1, 1966, Leimar continued to consult Mills on all questions regarding rates and they acted jointly in the revision and issuing of rate schedules.

Going back, the situation was that until May 1959 Mills and Leimar had this oriental import pool car business all to themselves.

At that time, as stated, a Victor Denning who was Traffic Manager for Mills in Montreal, left Mills and formed a new company called Denning Freight Forwarders Ltd., which entered into this west coast pool car business. This new company was financed by Milgram and Company which was a substantial Montreal broker, and the latter immediately caused certain importers in Montreal to employ the services of Denning, switching them from either Mills or Leimar.

As a result, Denning was successful in getting established in the business, and by early 1960, it had cut into the business of Leimar and Mills to such an extent that the latter two companies by agreement instituted a rate war in April 1960 which lasted until October of that year for the purpose of forcing Denning out of business. This rate

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war was referred to by Leimar and Mills in correspondence between them as "operation clobber".

This action of Leimar and Mills caused Denning in its 1960-61 operation in Vancouver in the short space of about six or seven months to lose about $32,000; and the evidence and allegation of Denning is that it was on the verge of bankruptcy at that time.

Denning, however, as a result, in June 1960 consulted a Toronto lawyer (see Exhibit 343). This lawyer advised three things, namely:

1. to approach the Board of Transport Commissioners of Canada to see if it could obtain some relief from that Board;
2. to approach the Restrictive Trade Practices Commission established under the *Combines Investigation Act* to see if some relief might be obtained; and
3. to institute a civil action for damages for conspiracy against Mills and Leimar.

All three things were done.

The Board of Transport Commissioners of Canada informed they did not have authority in this matter; the Restrictive Trade Practices Commission under the *Combines Investigation Act* advised they would look into the matter (and, as it transpired, did); and a civil action for damages for conspiracy was instituted against Mills and Leimar.

In October 1960, Mills and Leimar settled this civil action for conspiracy with Denning; and pursuant thereto entered into an agreement to pay Denning a commission for five years. (See Exhibit 284).

In this Agreement there was a release for damages for civil conspiracy.

At this time also, namely on October 27, 1960, Leimar wrote Mills and Kuehne & Nagel (Canada) Limited as follows:

> Whereas agreements were entered into between our companies under dates October 3, 1958 and October 7, 1958 and February 27, 1959 and
>
> Whereas neither you nor we have since the beginning of this year, or earlier, adhered to all the provisions of said agreements; and

> Whereas it has been suggested to us by counsel that such agreements during the period of their effectiveness may have been contrary to certain laws of Canada;
>
> We therefore now give notice that this company is not, and will not, be bound by the provisions of such agreements, which are hereby cancelled.

Attached to this letter is a hand-written note reading as follows:

> for the record only.

Mr. H. C. Boysen, Vice-President of Mills and Kuehne & Nagel (Canada) Limited replied to this letter of November 3, 1960, as follows:

> We hereby acknowledge receipt of your letter dated October 27 addressed to J. W. Mills & Son Limited and Kuehne and Nagel (Canada) Limited.
>
> We accept your notice to terminate the agreements between our companies, dated October 3, 1958, October 7, 1958 and February 27, 1959.
>
> It is agreed and understood that neither party shall be bound by the agreements after date of expiration.

On November 5, 1960, Mr. Boysen wrote to the President of Kuehne & Nagel Company in Germany in part as follows:

> In order to avoid an unnecessary sharp competition war Leith & Dyke and ourselves for the old Denning business, we have concluded a gentleman's agreement with Leith & Dyke. According to this agreement, we will for the time being only try to acquire the part of the old Denning business which we used to handle before, while Leith & Dyke will do the same thing with our old firms. This only applies for the transition period, after which Leith & Dyke and ourselves will try to handle as much business as possible in free competition. In this connection, we have agreed on (the) rates orally but not in writing, and our tariffs will be identical.
>
> On the advice of our lawyers, we have given notice to terminate our original agreement with Leith & Dyke of October 1958, because of the danger that, in the event of a investigation by Canadian authorities, this agreement would be termed illegal and we could perhaps be fined. We and Leith & Dyke agreed, however that even after the termination of the agreement we shall continue to adhere to its essential points.

Then in September 1960, as stated, Johnston Terminals Limited entered the Oriental import pool car business.

The first thing that Johnston did was to draw up a schedule of rates for imported freight by pool car to Montreal and Toronto, which rates were higher than the then current rates being charged by Leimar and Mills pursuant to their rate war with Denning, but lower than the rates which were in effect prior to the initiation of the rate war.

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Then in October 1960, Leimar and Mills got in touch with Johnston in an effort to get the latter to agree to quoting rates similar to and conforming with their rates.

There is great equivocation in the evidence as to what precisely was the result of these meetings.

But in the result, I am of opinion that although Johnston distrusted Leimar and Mills and was loathe to make an agreement with them, it did in fact agree at that meeting to publish a tariff and live by it in the future. In support of this for example, is the fact that Mr. Leith was able to foretell what was going to happen on November 7, 1960, namely, the publication of this tariff by Johnston (see Exhibit 119); also the General Manager of Johnston, Mr. Methven, after this meeting wrote the letter (Exhibit 123) in which he said he had agreed to the proposition above mentioned and the new rates of Johnston which it issued on November 7, 1960, were substantially the same as Leimar and Mills. (In this respect, the evidence of the defence witness Mr. Guest was based on railway cartage rates and did not touch the issue herein).

But other than that, Johnston did not cooperate or make any other agreements with Leimar and Mills and thereafter had nothing to do with them and competed in the normal way without any collusive arrangements with Leimar and Mills.

(In this latter connection, it is not without significance that Johnston did not succeed thereafter, at any relevant time, in obtaining more than 5 per cent of the market.)

One other company (not an accused), as also stated, attempted to enter this business, namely Freight Consolidators of Canada Limited, a company owned by certain customs brokers in Toronto. This company after three years of operation, was most unsuccessful in obtaining any significant part of the business in this market, and was supported by only three or four importers of any size. This company transported a very small amount of freight weekly during the three year period ending August 1, 1966, and most of it was by truck and in each case the trucker absorbed the O.C.P. differential, because the truckers did not enjoy the benefit of O.C.P. ocean rates.

Eighthly, there was another facet of this business during the material times, in which the accused Leimar and Mills were involved. The Canadian truckers attempted during the material times to obtain O.C.P. privileges, and made application to the Trans-Pacific Freight Conference of Japan for this purpose.

(The Railways through this Conference had obtained this O.C.P. rate many years ago.)

The Canadian truckers sought to secure from this Conference an identical arrangement of that enjoyed by the Railways.

Apparently in the United States the truckers have the same O.C.P. privileges.

But this Conference denied them this privilege and Leimar and Mills in connection with this truckers' application, (1) actively engaged in opposing the granting of such privilege to the Canadian truckers; and (2) as an alternative action in case their said opposition failed, Leimar and Mills made an attempt to control the business that would go by truck if such O.C.P. privilege was granted to any Canadian truckers' association.

But the Canadian truckers failed to obtain this O.C.P. rate privilege.

The purported reason why the Conference refused to grant O.C.P. privileges to the Canadian truckers was that there was no federal jurisdiction over truckers as there was over railways.[5]

Nevertheless, the truckers attempted to compete in this business.

Prior to 1962, trucker competition was not a substantial factor, but from 1962 on, the trucking companies endeavoured to increase their share of this market and by 1966 serviced approximately 20 per cent of this market. Apparently, to get such business, in each case, the truckers absorbed the differential of the O.C.P. rates.

What happened in the result was that, during the material times, 80 per cent of the articles or commodities listed in Tariffs 70A, 70B and 70C imported from the said designated areas in the Orient to the Port of Vancouver

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[5] Following the decision of the Privy Council in *Attorney-General for Ontario v. Israel Winner et al* [1954] A.C. 541, holding inter-provincial transportation a matter of federal legislative jurisdiction under section 92(10)(*a*) of the *British North America Act, The Motor Vehicle Transport Act* 1953-54 (Can.) c. 59 was passed, which, *inter alia*, delegated to the provincial motor vehicle licensing bodies, authority to license trucks engaged in inter-provincial business.

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were transported to Toronto and Montreal by railway car; and of that 85 per cent of this business was serviced by the freight forwarders, the balance of 15 per cent being done by individual consignees on their own; and of this 85 per cent Johnston did 5 per cent of this business, Freight Consolidators of Canada Limited did a negligible percentage, and the balance was handled by Leimar and Mills.

Both the accused and the Crown made certain admissions. They were as follows:

(a) by the accused:

(i) Admissions (Exhibit 1)

ADMISSIONS

(Exhibit 1)

Pursuant to Section 562 of the Criminal Code, Statutes of Canada, 1953-54, Chapter 51, the accused admit the following facts:

1. That each Company or Corporation mentioned in the Indictment as an accused or as a co-conspirator is a legal entity with corporate existence and, accordingly, is a person as defined in the Criminal Code and more particularly that:

(a) *J. W. MILLS & SON, LIMITED*—incorporated under the provisions of the "Companies Act", R.S.C. 1906 by Letters Patent dated March 21, 1922 with its head office situate in Montreal, in the Province of Quebec.

(b) *KUEHNE & NAGEL (CANADA) LIMITED*—originally incorporated under the name K & N TRANSPORT LIMITED under the provisions of the "Companies Act", R.S.C. 1934, by Letters Patent dated April 21, 1953 with supplementary Letters Patent dated June 30, 1954 changing the name to Kuehne & Nagel (Canada) Limited with its head office situate in Montreal in the Province of Quebec.

(c) *OVERLAND IMPORT AGENCIES LTD.*—operating under the name LEIMAR FORWARDING CO. from June 12, 1964 and originally incorporated under the name MARDOCK ENTERPRISES LTD. under the provisions of the "Companies Act", R.S.B.C. 1960 by Certificate of Incorporation dated August 1, 1962 with a Certificate of Change of Name changing the name to Overland Import Agencies Ltd. dated August 7, 1964 and with its registered office situate in Vancouver, in the Province of British Columbia.

(d) *DENNING FREIGHT FORWARDERS LTD.*—incorporated under the provisions of the "Companies Act", R.S.C. 1952 by Letters Patent dated May 1, 1959 with its head office situate in Montreal, in the Province of Quebec.

(e) *JOHNSTON TERMINALS LIMITED*—incorporated under the provisions of the "Companies Act", R.S.B.C. 1936 by Certificate of Incorporation dated December 28, 1945 with its registered office situate in Vancouver in the Province of British Columbia.

(f) *LEITHDYKE FORWARDERS LIMITED*—incorporated under the provisions of the "Companies Act", R.S.B.C. 1948 by Certificate of Incorporation dated July 20, 1956 with its registered office situate at Vancouver, in the Province of British Columbia.

(g) *THOMAS MEADOWS & COMPANY CANADA, LIMITED*—incorporated under the provisions of the "Companies Act", R.S.C. 1906 by Letters Patent dated July 29, 1920 with its head office situate in Toronto, in the Province of Ontario.

(h) *LEITH SERVICES LTD.*—(presently in Voluntary Liquidation) incorporated under the provisions of the "Companies Act", R.S.B.C. 1948 by Certificate of Incorporation dated July 24, 1959 with its registered office situate in Vancouver, in the Province of British Columbia and MARDOCK ENTERPRISES LTD. carrying on business under the firm name and style of LEIMAR FORWARDING CO. which said partnership was registered under the "Partnership Act", R.S.B.C. 1960 by Declaration of Partnership registered September 1, 1962 in the County Court of Vancouver and which said partnership was dissolved by a Declaration of Dissolution of Partnership dated June 12, 1964 and which Declaration of Dissolution was registered in the County Court of Vancouver on June 12, 1964.

(i) *MUIRHEAD FORWARDING LIMITED*—incorporated under the provisions of the "Companies Act", R.S.C. 1934 by Letters Patent dated May 23, 1947 with its head office situate in Toronto, in the Province of Ontario.

2. That each of the persons listed below was an officer or agent or servant or employee or representative of the Company or Corporation under which his name is listed, during the period covered by the Indictment or during a portion of the said period:

(a) *J. W. MILLS & SON, LIMITED* and *KUEHNE & NAGEL (CANADA) LIMITED*

	Name	*Capacity*
Germany—		
	Alfred Kuehne	President
	K. M. Kuehne	
	L. Roessinger	
	L. Lueck	
Montreal—		
	Horst G. Schellak	Vice President
	Peter Ptacek	Sales Representative
	Janus	
Toronto—		
	Hans Christian Boysen	Vice President Manager Managing Director
	Gurd H. Stoppenbrink	Secretary-Treasurer
	H. A. Gutke	Manager

	Name	*Capacity*
Vancouver—		
	Fred Schultze	Manager
	Peter Reschke	Manager
	Ray W. Bos	
	J. Pusch	
	Michael von der Nuell	
Winnipeg—		
	R. B. Locher	
Hamilton—		
	Wilkie	

(b) *OVERLAND IMPORT AGENCIES LTD. (LEIMAR FORWARDING CO.)*

	Name	*Capacity*
Vancouver—		
	R. Stanley Leith	President
	Ian Mardock	Vice-President
		Manager
		President
	William Doig	
	James Greenlees	

(c) *DENNING FREIGHT FORWARDERS LTD.*

	Name	*Capacity*
Montreal—		
	Victor J. Denning (Dening)	President
	Nathan Gross	Vice-President
	Harry Milgram	Shareholder
	Fred Zanders	
	Bernard Gross	
	Gerald Gross	
	Oscar Goldman	
Toronto—		
	Mrs. H. L. Weiss	
Vancouver—		
	Tom Dombay	Manager

(d) *JOHNSTON TERMINALS LIMITED*

	Name	*Capacity*
Vancouver—		
	James N Methven	Vice-President
		Assistant General Manager
		General Manager
	Douglas M. Brown	Vice-President & Managing Director
	R. Murray Brink	Director
	Bill E McKinney	Sales Manager
	Peter L Richardson	Foreign Freight
	Vic Shiedel	Import Department
	Ralph Mattson	
	I Froese	

(e) *LEITHDYKE FORWARDERS LIMITED (LEITH SERVICES LTD. & LEIMAR FORWARDING CO)*

	Name	Capacity
Vancouver—		
	R. Stanley Leith	President
	Ian F. Mardock (formerly Gee)	Manager
	William Doig	Assistant Manager
	F. G. Smith	Vice-President
	J. M. Brill	Canvasser
	David Leith Edwards	
	Percy H. Dyke	
	B. L. O'Malley	
	Roy Johnston	
	James Greenlees	
	Ronald Richards	

(f) *THOMAS MEADOWS & COMPANY CANADA, LIMITED*

	Name	Capacity
Montreal—		
	Frank O'Rourke	Managing Director
	J. V. Mitchell	Manager
	Ray Delaney	Canvasser
	Winger	Canvasser
	T. J. Dombay	Staff Member—Leimar
	Harry Wegner	
	Pat J. Parsons	
	Foley	
Toronto—		
	Arthur R. Carey	President
	J. W. Sedge	Managing Director
	Peter Stonebanks	Joint Manager
	L. C. Nicholls	in charge of Leimar
Winnipeg—		
	Hans Haase	Manager—Leimar
	Morris Hoshowski	

(g) *MUIRHEAD FORWARDING LIMITED*

	Name	Capacity
Montreal—		
	Herb L. Duerr	Manager
	Charles Osborne	
	Joe Williams	
Toronto—		
	Robert E. Vince	Assistant General Manager
	Jack D. Fraser	
Hamilton—		
	E. M. Perkins	

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3. That the documents described herein, the originals of which are to be produced by Counsel for the Crown for admission as evidence under Section 41 of the Combines Investigation Act, R.S.C. 1952, Chapter 314, were obtained from (i) the possession of the accused Companies or Corporations or those named as co-conspirators, or (ii) on premises used or occupied by the said accused Companies or Corporations or co-conspirators, as cited below:

(a) *J. W. MILLS & SON, LIMITED and KUEHNE & NAGEL (CANADA) LIMITED*

Montreal	—serial nos. 439 to 1048 inclusive
	—serial nos. 6000 to 8163 inclusive
Toronto	—serial nos. 120 to 438 inclusive
	—serial nos. 9176 to 9963 inclusive
Vancouver	—serial nos. 3290 to 4073 inclusive
	—serial nos. 10661 to 11129 inclusive

(b) *OVERLAND IMPORT AGENCIES LTD., LEIMAR FORWARDING CO., LEITHDYKE FORWARDERS LIMITED, IAN F. MARDOCK (formerly known as Ian F. Gee), the late R. Stanley Leith and LEITH SERVICES LTD.*

Vancouver	—serial nos. 2082 to 3289 inclusive
	—serial nos. 4228 to 4545 inclusive
	—serial nos. 4840 to 5964 inclusive
	—serial nos 10015 to 10660 inclusive

(c) *DENNING FREIGHT FORWARDERS LTD.*

Montreal	—serial nos. 1555 to 2081 inclusive
	—serial nos. 4546 to 4579 inclusive
	—serial nos. 8164 to 8416 inclusive

(d) *JOHNSTON TERMINALS LIMITED*

Vancouver	—serial nos. 4074 to 4227 inclusive
	—serial nos. 11130 to 11328 inclusive

(e) *THOMAS MEADOWS & COMPANY CANADA, LIMITED*

Toronto	—serial nos. 1-119 inclusive
	—serial nos. 8671-9175 inclusive
Montreal	—serial nos. 1049-1554 inclusive
	—serial nos. 8417-8670 inclusive

(f) *MUIRHEAD FORWARDING LIMITED*

Toronto	—serial nos. 4580-4839 inclusive
	—serial nos. 9964-10014 inclusive
Montreal	—serial nos. 11329-11368 inclusive

(ii) Admissions (Exhibit 14)

ADMISSIONS
(Exhibit 14)

Pursuant to Section 562 of the Criminal Code, Statutes of Canada, 1953-54, Chapter 51, the accused admit the following facts:

1. That during the period described in the Indictment eighty (80%) percent—ninety-five (95%) percent of all import pool car traffic coming within the terms of Canadian Freight Association tariffs 70A, 70B and 70C was carried by the Canadian National Railway and the Canadian Pacific Railway.

2. That during the period described in the Indictment approximately eighty-five (85%) percent of all import pool car traffic referred to in Paragraph 1 was handled by the accused corporations, but the portion of the traffic handled by the defendant, Johnston Terminals Limited, was less than three (3%) to five (5%) percent of the total traffic handled by the accused corporations.

(iii) Admissions (Exhibit 14A)

ADMISSIONS
(Exhibit 14A)

Pursuant to Section 562 of the Criminal Code the accused Corporations admit the following:

That during the period described in the Indictment not more than twenty (20%) percent of those articles or commodities imported from the designated area, described in Tariffs 70A, 70B and 70C and routed through the port of Vancouver, which could have been transported by rail in railway pool cars to points in Eastern Canada, east of the Manitoba-Ontario Boundary to the City of Toronto and elsewhere in the Province of Ontario, and to the City of Montreal and elsewhere in the Province of Quebec, were carried by truck transport.

(b) by the Crown:

(i) Admissions (Exhibit 18)

ADMISSIONS
(Exhibit 18)

Pursuant to the Criminal Code Statutes of Canada, 1953-54, Chapter 51, the Crown admits the following:

1. That all truck tariffs published and approved by valid provincial legislation are to be admitted without formal proof.

2. That the tables prepared from Dominion Bureau of Statistics Records attached hereto and numbered 1 to 6, shall be admitted without formal proof.

3. That the volume of traffic handled pursuant to C.F.A. tariffs 70A, 70B and 70C constitute only a small portion of the imports from the area designated in tariffs 70A, 70B and 70C.

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Imports by Weight from Selected Countries

TAIWAN

(tons—2,000 lbs)

Year	Atlantic Ports	Great Lake Ports	Pacific Ports	Total
1965	7,967	2,883	15,281	26,131
	30 5%	11%	58.5%	100%
1964	9,217	2,458	11,621	23,296
	39 5%	10 5%	50%	100%
1963	3,957	989	10,706	15,652
	25%	6%	69%	100%
1962	1,883	100	4,540	6,523
	29%	1 5%	69 5%	100%
1961	345	—	4,786	5,131
	7%	—	93%	100%
1960	2	—	2,016	2,018
			100%	100%
1959	5	—	310	315
			100%	100%
1958	—	—	—	—
1957	—	—	—	—
1956	—	—	—	—

Reference: "Cargoes Unloaded at Canadian Ports from Foreign Countries" from *Shipping Report, 1956-65,* Dominion Bureau of Statistics, Queen's Printer, Ottawa.

Imports by Weight from Selected Countries

KOREA

(tons—2,000 lbs)

Year	Atlantic Ports	Great Lake Ports	Pacific Ports	Total
1965	23	—	1,145	1,168
	2%	—	98%	100%
1964	—	18	686	704
	—	2 5%	97 5%	100%
1963	270	—	219	489
	55%	—	45%	100%
1962	363	463	74	900
	40 5%	51 5%	8%	100%
1961	—	—	1	1
	—	—	100%	100%
1960	—	—	—	—
	—	—	—	—
1959	—	—	—	—
	—	—	—	—
1958	—	—	—	—
	—	—	—	—
1957	—	—	—	—
	—	—	—	—
1956	—	—	—	—

Reference: "Cargoes Unloaded at Canadian Ports from Foreign Countries" from *Shipping Report, 1956-65,* Dominion Bureau of Statistics, Queen's Printer, Ottawa.

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Imports by Weight from Selected Countries
CHINA—MAINLAND
(tons—2,000 lbs)

Year	*Atlantic Ports*	*Great Lake Ports*	*Pacific Ports*	*Total*
1965	—	170	19,440	19,610
	—	1%	99%	100%
1964	848	190	6,023	7,061
	12%	3%	85%	100%
1963	2,153	56	2,086	4,295
	50%	1 5%	48 5%	100%
1962	1,263	—	1,844	3,107
	40 5%	—	59 5%	100%
1961	16	—	1,399	1,415
	1%	—	99%	100%
1960	34	—	4,771	4,805
	1%	—	99%	100%
1959	—	—	903	903
	—	—	100%	100%
1958	468	—	5,563	6,031
	7 5%	—	92%	100%
1957	34	—	1,357	1,391
	2 5%	—	97 5%	100%
1956	48	—	70	118
	40%	—	60%	100%

Reference: "Cargoes Unloaded at Canadian Ports from Foreign Countries" from *Shipping Report, 1956-65,* Dominion Bureau of Statistics, Queen's Printer, Ottawa.

Imports by Weight from Selected Countries
HONG KONG
(tons—2,000 lbs)

Year	*Atlantic Ports*	*Great Lake Ports*	*Pacific Ports*	*Total*
1965 ..	14,775	2,652	22,325	39,752
	37%	7%	56%	100%
1964 ..	6,555	2,486	18,450	27,491
	24%	9%	67%	100%
1963 ..	7,134	1,434	15,183	23,751
	30%	6%	64%	100%
1962 ..	3,426	1,300	15,396	20,122
	17%	6 5%	76.5%	100%
1961 ..	1,661	980	12,417	15,058
	11%	6 5%	82 5%	100%
1960 ..	2,655	365	12,350	15,370
	17%	2 5%	80.5%	100%
1959 ..	2,211	—	9,768	11,979
	18 5%	—	81 5%	100%
1958 ..	835	—	9,952	10,787
	7 5%	—	92 5%	100%
1957 ..	1,317	—	12,096	13,413
	10%	—	90%	100%
1956 ..	817	—	23,069	23,886
	3%	—	97%	100%

Reference: "Cargoes Unloaded at Canadian Ports from Foreign Countries" from *Shipping Report, 1956-65,* Dominion Bureau of Statistics, Queen's Printer, Ottawa

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Imports by Weight from Selected Countries

JAPAN

(tons—2,000 lbs.)

Year	*Atlantic Ports*	*Great Lake Ports*	*Pacific Ports*	*Total*
1965 ..	130,803	42,747	339,672	513,222
	25 5%	8.5%	66%	100%
1964 ..	76,329	24,683	252,684	353,696
	22 5%	7%	70 5%	100%
1963 ..	48,787	20,538	172,721	242,046
	20%	8 5%	71.5%	100%
1962 ..	52,336	11,842	177,747	241,925
	21 5%	5%	73 5%	100%
1961 ..	41,786	11,204	152,916	205,906
	20%	5 5%	74 5%	100%
1960 ..	28,765	9,775	168,103	206,643
	14%	4 5%	81 5%	100%
1959 ..	31,510	710	189,444	221,664
	14%	—	86%	100%
1958 ..	2,299	—	100,942	103,241
	2%	—	98%	100%
1957 ..	3,126	—	123,998	127,124
	2 5%	—	97.5%	100%
1956 ..	3,341	—	170,455	173,796
	2%	—	98%	100%

Reference: "Cargoes Unloaded at Canadian Ports from Foreign Countries" from ***Shipping Report, 1956-65,*** Dominion Bureau of Statistics, Queen's Printer, Ottawa.

Value of Imports from Selected Foreign Countries
In Dollars

Year	*Taiwan*	*Japan*	*Hong Kong*	*China-Mainland*	*Korea*
1966 .	13,088,532	253,050,976	38,910,541	20,594,268	1,763,824
1965 . .	9,332,994	230,144,052	31,042,884	14,445,013	1,467,630
1964	9,063,491	174,388,169	26,321,470	9,420,133	473,128
1963 . . .	5,875,412	130,471,048	21,197,324	5,146,500	380,381
1962	2,909,523	125,358,920	18,889,385	4,521,079	98,721
1961 .	1,856,204	116,607,360	14,143,178	3,232,588	76,212
1960 .	1,150,222	110,382,498	15,534,055	5,638,180	404,499
1959 .	715,812	102,669,366	12,969,338	4,840,377	235,026
1958	159,466	70,215,591	8,822,749	5,375,607	24,276
1957 . . .	192,743	61,604,709	7,223,021	5,314,243	34,829
1956	111,655	60,826,294	5,699,077	5,721,189	8,377

Reference: ***Trade of Canada,*** 1956-66, Dominion Bureau of Statistics, **Queen's Printer, Ottawa.**

(ii) Admissions (Exhibit 18A)

ADMISSIONS

(Exhibit 18A-

Amending Exhibit 18)

Pursuant to the Criminal Code Statutes of Canada, 1953-54, Chapter 51, the Crown admits the following·

1. That all truck tariffs published and approved by valid provincial legislation are to be admitted without formal proof.

2. That the tables prepared from Dominion Bureau of Statistics Records attached hereto and numbered 1 to 6, shall be admitted without formal proof.

3. That the volume of traffic handled pursuant to C F A. tariffs 70A, 70B and 70C constitute only a small portion of the imports *to Canada as a whole of the nature described therein* from the area designated in tariffs 70A, 70B and 70C.

(iii) Admissions (Exhibit 302)

ADMISSIONS

(Exhibit 302)

Pursuant to the Criminal Code Statutes of Canada, 1953-54, Chapter 51, the Crown admits the following.

1. That all the persons, firms or corporations, who appointed the accused, J W. Mills & Son, Limited, Kuehne & Nagel (Canada) Limited, Overland Import Agencies Ltd, or Denning Freight Forwarders Ltd. agents by executing and delivering a General Authorization, carried on business in and about the City of Toronto, in the Province of Ontario or the City of Montreal, in the Province of Quebec.

2. That each of the said accused, J W Mills & Son, Limited, Kuehne & Nagel (Canada) Limited, Overland Import Agencies Ltd, and Denning Freight Forwarders Ltd, maintained sales offices or agents for solicitation and other purposes related to the business carried on by the said accused in the said City of Toronto and the said City of Montreal during the whole of the period described in the said Indictment and during the period that the accused carried on business

3 That persons representing owners of transportation namely, trucks, aircraft and vessels operating into the ports of New York, N Y, Halifax, Nova Scotia; St John, New Brunswick; Montreal, Quebec; and Toronto, Ontario, also solicited the principals of the accused during the period covered by the Indictment.

This evidence establishes that the accused Leimar, Mills and Kuehne & Nagel (Canada) Limited, by their collusive actions obtained substantial market power (or bargaining power) in the market in which they operated their

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respective businesses. In particular, in considering this, the factual situations that obtained at the following times are significant, that is to say:

(a) in October 1958, the time of the Mills and Leimar agreements;

(b) in October 1960, the time of the Denning agreement with Leimar and Mills in settlement of the civil action for conspiracy; and

(c) the period after November 1960, the date of the Johnston agreement with Leimar and Mills, to August 1, 1966, during which period Johnston had no success in obtaining an appreciable percentage of the business in this market, and Freight Consolidators of Canada Limited had practically no success at all.

So much for the facts.

As to the law, the two broad issues for adjudication in this case require:

(1) a determination of whether or not the Indictment and the Particulars thereof alleges and the evidence adduced has proven in this criminal trial a correct relevant competitive market; and

(2) whether the behaviour or conduct of the accused in such relevant market in its collusive aspects during the alleged period of time had the element of "undueness" so as to constitute an offence under section 32(1)(*a*) of the *Combines Investigation Act* or under section 32(1)(*c*) of the Act, or both.

Speaking generally, as I understand it, the pertinent legislative purpose of the said subsections of the Act, and evidence necessary to prove breaches of them may be put in this way:

The legislative purpose of both sections 32(1)(*a*) and 32(1)(*c*) of the *Combines Investigation Act* relate to lessening of "competition" "unduly", and is to protect the public interest in "free competition" as judicially understood.

In the cases there have been many attempts to define "unduly" but in none of the cases have the Courts laid down any specific portion of the relevant market that must be accounted for by the parties to any anticompetitive trade practice or policy to prove an offence has been committed.

Also there has been no reference to what the Canadian Courts mean by competition except that it must be "free competition".

Nevertheless, the concept of "competition" is central to the determination of whether or not an offence has been committed contrary to section 32(1)(*a*) or section 32(1)(*c*) of the *Combines Investigation Act,* because in relation thereto, the Courts in Canada rely on the *market* to give the kind of business "competition" considered desirable.

As a consequence, in every adjudication under these subsections of the Act there is an examination of two competitive features in their collusive aspects and these relate to (1) the market structure and (2) the behaviour or conduct of the participants; and in respect to both, the way in which the "relevant market" is defined, is of the essence.

(In most cases, however, the problem of defining the relevant market is not too difficult. Illustrative of this are the decisions in a number of Canadian cases where the relevant market was defined by reference to only two characteristics or dimensions, namely, commodities and geography (see cases in Schedule "B"). In such cases it was not necessary for the purpose of defining the relevant market to engage in prolonged economic investigations and to adduce lengthy evidence in respect thereto. Indeed, also even in cases where the problem of defining the relevant market is complex, as for example, either in product (or service) or geographical characteristics or dimension, adequate evidence is usually available from the business records seized and put in evidence (for the purpose of section 41 of the *Combines Investigation Act*[6]. Very often also the conspiracy or combination itself delineates the relevant market with sufficient clarity.

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[6] See, e.g., how Duff J., as he then was, defined "the relevant market" in terms of both commodity and geography in the case of *Mordecai Weidman et al v. Bernard Shragge* (1912) 46 S.C.R. 1 at p. 37, viz: "in an important article...throughout a considerable extent of territory".

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In cases where this does not obtain, some economic evidence may be necessary.

In the subject case, the defence led with economic evidence and there was substantial cross-examination. Evidence was given of many of the usual characteristics or dimensions which sometimes should be considered in defining a relevant market. And in these reasons, consideration is given to these characteristics or dimensions generally and to the specific ones which the parties in evidence and argument relied on in defining what, in their respective submissions, was the relevant market in this case.)

The examination for the purposes of section 32(1)(*a*) and section 32(1)(*c*) of the *Combines Investigation Act* of (1) the market structure, and (2) the behaviour or conduct of the participants, as I understand it, may be done (i) by ascertaining whether or not a relevant market has been alleged in the Indictment and Particulars and has been proven; and then (if alleged and proven) (ii) by considering the behaviour or conduct of the participants in such relevant market, to ascertain whether "undueness" has been proven. The onus of proof on the Crown, of course, in relation to both matters, is the usual onus in any criminal prosecution.

Re the relevant market

In examining and assessing the competitive feature of the market structure, what is pertinent is the boundaries of the market because the determination of what competition is relevant is one of the key issues, and unless the relevant market in every case is defined it is not possible to weigh the element of "undueness" in any factual situation within the purview of section 32(1)(*a*) of section 32(1)(*c*) of the *Combines Investigation Act.*

As Laskin J. stated in *The Queen v. K. J. Beamish Construction Company Limited* (Court of Appeal of Ontario, unreported):

> Undueness in any agreed upon scheme of lessening competition in, for example, the sale, transportation or supply of an article, involves advertence to the area of operation of the competition in question. An agreement to lessen competition unduly in respect to the matters defined in section 32(1)(*c*) must be assessed in relative terms. The very notion of competition which the Act undergirds envisages a market within which it may operate without an illegal agreement of restriction.

As a matter of law of course there is no definition of the "market" in relation to which the evidence of any alleged violation of sections 32(1)(*a*) and 32(1)(*c*) of the *Combines Investigation Act* may be examined. What is the relevant market in every case is a matter of judgment based upon the evidence.

As Laskin J. also put in the said case:

> It is obvious that a Court may be required to exercise a judgment on the evidence on whether the market specified in the indictment or the particulars, or of which proof is accordingly made, has not been artificially limited to suit the available evidence

For analogous purposes, other salutary words have also been employed elsewhere in respect to other statutes, in cautioning the prosecution not to tailor the market artificially to fit a subject case. (See Schedule "C").

(There is also no legal definition capable of describing the shape of competition. This is a changing matter (as for example, new products may come into direct competition, or service requirements re-arrange the geographical nature of a particular market).)

But speaking generally, it is of importance to bear in mind that the term "market" is a relative concept. In one sense, there is only one market in an economy since, to some extent, all products and services are substitutes for each other in competing for the customer's dollar.

In another sense, almost every firm has its own market since, in most industries, each firm's product is differentiated, to some extent, from that of all other firms.

Defining the relevant market in any particular case, therefore, requires a balanced consideration of a number of characteristics or dimensions to meet the analytical needs of the specific matter under consideration.

At one extremity, an ill-defined description of competition is that every service, article, or commodity, which competes for the consumer's dollar is in competition with every other service, article, or commodity.

At the other extremity, is the narrower scope definition, which confines the market to services, articles, or commodities which have uniform quality and service.

In analyzing any individual case these extremes should be avoided and instead there should be weighed the various factors that determine the degrees of competition and the

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dimensions or boundaries of the competitive situation. For this purpose the dimensions or boundaries of a relevant market must be determined having in mind the purpose for what it is intended. For example, two products may be in the same market in one case and not in another.

And many characteristics or dimensions may be considered in defining the relevant market. All are not of the same order. And, in any particular case, usually, not all of the many characteristics or dimensions will have to be considered. In some instances, the definition may turn on only one characteristic or dimension or two (see again cases in Schedule "B"). However, in order to make a correct choice of the appropriate characteristics or dimensions, it may be necessary to review several types before selecting the proper one or ones.

Hereunder are noted some pertinent characteristics or dimensions that may be considered in defining a relevant market, but this list is not exhaustive. The classification also may be arranged in various ways.

(a) Product substitutability.

(The term economists use for this is "cross-elasticity of demand". The terms "substitutability" and "cross-elasticity" are synonymous. As an example, the demands for two products have a high cross-elasticity if a change in the price of one results in a large measure, in purchasers substituting it for the other. How to measure the degree of cross-elasticity in any given case is usually difficult.)

(b) Actual and potential competition.

(The problem sometimes in competition analysis is whether to confine the "relevant market" to existing competition or to consider potential (sometimes called "poised") competition as well).

(c) Geographical area.

(The geographical dimensions of a market are frequently an important factor in competitive analysis —e.g., should the relevant market be analyzed on a national basis, a regional or local area).

(d) Physical characteristics of products or service. (Selecting products that have the same physical characteristics, or services that have the same features, is the simplest basis for defining a relevant market. But in some cases, for example, it may be correct legally to consider products with fairly dissimilar physical characteristics or services with somewhat dissimilar elements, as in the same market).

(e) End uses of products.

(The factor of end uses is closely related to physical characteristics in defining the relevant market. For example, if a product has different end uses in the hands of buyers, the definition of the relevant market may not be based solely on physical specifications. Also, for example, consideration of differences in uses is particularly important in studying markets for services).

(f) Relative prices of goods or services.

(The prices of goods or services may define the relevant market).

(g) Integration and stages of manufacture.

(Because of differences between the activities of competitors, problems of integration arise. In determining the relevant market, the problem is what products at what stage of manufacture to include or exclude).

(h) Methods of production or origin.

(Methods of production and the product resulting, and origin of material, as e.g., whether or not imported, are often important factors to consider in defining the relevant market).

Having employed some or all of the above significant characteristics or dimensions in making a judgment as to what is the relevant market in a particular case, the Court may in some cases then wish to consider some or all of the following additional features or indicators of the structural characteristics of such relevant market for the purpose of testing whether or not strong monopoly elements could endure, i.e. in weighing whether or not "undueness", could be proven under any factual situation, that is to say:

1. The number and concentration of competition.

(This criterion covers the number of firms and their relative sizes. It often, however, does not provide a direct measure of the degree of competition.)

2. Barriers to entry.

(The relative ease or difficulty of entry into a market by a new firm is a prime factor in analyzing market structure. Generally speaking, if there are no substantial barriers to entering a market, strong monopoly elements will have great difficulty enduring, and conversely.)

3. Geographical distribution of buyers and sellers.

(Transportation costs are probably the most important factor in this element of market structure).

4. Differences in the degree of integration of competition.

(This matter arises when some competitors supply their own products or services while others are required to sell or purchase those same products or services. The former competitors at some stage of manufacture may have the power to squeeze its unintegrated competitor between high costs and low selling prices. Integration can also affect differences in competitors' costs.)

5. Product differentiation.

(Every firm seeks if possible, to build its own monopoly of a market by product differentiation. In this they are sometimes assisted through the use of trade marks and design features. The significance of product differentiation is dependent upon consumer information concerning product qualities and features.)

6. Countervailing power.

(This factor is sometimes difficult to measure. Its mere existence, however, may reflect substantial anti-competitive elements in the market. For example, the fact that one large firm has the ability to manufacture an article or a commodity may substantially limit the monopoly power of the established firm manufacturing such articles or commodities).

7. And again, cross-elasticity of demand.

(Because such affects both the nature of the competition within the relevant market, and also the definition of the relevant market).

Re the behaviour or conduct of the participants in the relevant market.

In examining and assessing the competitive feature of the behaviour or conduct of the participants in a relevant market, in its collusive aspects, what is germane since the 1960 amendment to the *Combines Investigation Act* is to consider the proof of any of the "devices" which were contemplated being employed (or also, if applicable, the employment of any of them) by the parties to any alleged conspiracy, combination, agreement or arrangement, relating to one or more of the following: (a) prices, (b) quantity or quality of production, (c) markets or customers, (d) channels or methods of distribution, and (e) if the proof does not relate to any of the devices listed in section 32(2)(*a*) to (*g*) and section 32(3)(*a*) to (*d*) of the Act, then to proof that the parties contemplated employing (and if applicable, employed) some other "device" which had as its result, that "the conspiracy, combination, agreement or arrangement...restricted or is likely to restrict any person from entering into or expanding a business in a trade or industry".

(In relation to both this competitive feature, and the other competitive feature, market structure, it may be observed that proof of the behaviour or conduct of the sellers in the relevant market in most cases under the *Combines Investigation Act* is usually much more extensive than proof of the other competitive feature, firstly because it is more frequently the more substantial issue, and secondly, because such proof fits into the process of litigation by the adversary system more readily.

But it is also important to bear in mind that behaviour or conduct features are not clearly distinct from the market structure features. Some aspects of structure may be so dependent on behaviour, that lines of demarcation between the two must be arbitrary.

In addition, it should also be noted that analysis of behaviour or conduct of sellers frequently calls for consideration of the conduct of buyers as well.)

So much for the legislative purpose and evidence necessary to prove breaches of these subsections of the Act.

The specific defences of each of the accused are now considered.

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The facts concerning Denning are sufficiently set out above.

In essence, the submission of Denning (in addition to the defence submission of the accused Leimar and Mills and Kuehne & Nagel (Canada) Limited, hereinafter referred to, which it also adopted) was that in June, 1959 it entered into the freight forwarding business in Vancouver; in 1960 was subject to a rate war conducted against it by Leimar and Mills which resulted in loss in its Vancouver operation of $32,000 in six or seven months causing it to be on the brink of bankruptcy; that in respect to this said predatory action of the accused Leimar and Mills it instituted a civil action against them for damages for civil conspiracy which was settled in October 1963 by formal agreement which agreement was in release of all damages for the claim for civil conspiracy and provided for a method of paying the damage settlement agreed upon[7]; that by one of the terms of this agreement it could be renewed after the expiry of the term of it namely, five years, at which time, if not renewed, Denning was free to re-enter the freight forwarding business, but if renewed for a period of one further year, Denning would be paid a commission of 15 per cent on business contracted.

In my view, considering the whole of the evidence, such does not constitute an offence by Denning Freight Forwarders Limited either under Count 1 or Count 2; and therefore it is not necessary to consider in relation to this accused the additional defence of the accused Mills, Kuehne & Nagel (Canada) Limited and Leimar, which it adopted, and as a consequence Denning Freight Forwarder Limited is acquitted.

In respect to Johnston Terminals Limited, it also adopted the defence submission of Leimar and Mills, but in addition, it submitted that at no time did it conspire or agree with Leimar or Mills about anything.

The facts concerning Johnston are also sufficiently set out above.

On these facts, I am of opinion that Johnston Terminals Limited in October 1960 did agree with Leimar and Mills

[7] cf. Thompson J. in *Trim Trends Canada Limited v. Dreomatic Metal Products Limited et al*, Supreme Court of Ontario, 29 September, 1967, unreported.

to publish a tariff and live by it in the future; and that in pursuance of that agreement they did publish a tariff with roughly equivalent rates to those of the tariffs of the accused Leimar, Mills and Kuehne & Nagel (Canada) Limited. Johnston was at that time just getting into this business and, it is a reasonable inference, probably agreed to this in part because it was not familiar with the actual costs to it of carrying on this business. Other than that Johnston did not engage in any anti-competitive trade practice or policy with Leimar and Mills and by 1961 was in "free competition" with Leimar and Mills as those words are understood by the courts.

The only other matter to consider in relation to this accused (other than the defence submission of the accused Leimar and Mills which Johnston adopted) is whether what Johnston did had the necessary criminal element of "undueness" so as to constitute an offence under Count 1 or Count 2 or both. Without detailing all of the *indicia* which are apparent from the facts already set out, I am of opinion, on considering the whole of the evidence, that what Johnston did, did not have such necessary element either under Count 1 or Count 2; and therefore it is also not necessary to consider in relation to the accused the additional defence of the accused Mills, Kuehne & Nagel (Canada) Limited and Leimar which Johnston adopted, and as a consequence, Johnston Terminals Limited is acquitted.

The defence of the accused Mills, Kuehne & Nagel (Canada) Limited and Leimar was twofold namely:

1. that the Crown in the Indictment and Particulars thereof did not allege and define a true and realistic competitive market but instead in this respect (in the words of counsel for Leimar) did some "economic gerrymandering" in defining what it considered the relevant market; and

2. that if the Indictment and Particulars had specified the true competitive market that the elements of what the accused did lacked the necessary criminal element of "undueness" as relating to:

   (i) limiting "the facilities for transporting" etc., (section 32(1)(*a*) of the *Combines Investigation Act*); and also

(ii) the prevention or lessening of "competition in transportation" etc. (section 32(1)(*c*) of the Act).

The defence witnesses relating to the relevant market were Dr. James Alexander Sherbaniuk, an economist of Simon Fraser University called by counsel for Mills; and Mr. K. R. Woodcock of Canadian Pacific Railways, Mr. Whalen of a steamship company which did business transporting articles and commodities from the Orient to the Port of Vancouver among other places, Mr. W. R. Sparks of Eatons of Canada Limited, Mr. I. F. Mardock, President of Mills and Mr. S. H. Garrod of the Canadian Pacific Railways, all of whom were called by counsel for Leimar.

The purpose of their evidence was to attempt to show that the relevant market in which these accused operated their businesses was not confined to articles or commodities defined in said Tariffs 70A, 70B and 70C, imported from the said designated area of the Orient, and shipped by sea to the Port of Vancouver and by rail in mixed carloads or by truck to Toronto or Montreal; but instead included in addition a much greater range of articles and commodities which were shipped by all manner of vessels from the Orient to either New Orleans, New York, Halifax, Montreal or Toronto and also where applicable, were trucked from these Ports to importers in Toronto and Montreal; and in addition included air traffic transportation of articles or commodities from the Orient to importers in Toronto and Montreal. In the defence economic evidence of Dr. Sherbaniuk, adduced to prove this, he stated that the following of the above mentioned characteristics or dimensions were significant in defining the relevant market as envisaged by the defence, namely: (*a*) product substitutability (cross-elasticity of demand), (*b*) actual and potential "poised" competition, and (*c*) geographical area.

These accused also sought to establish by their evidence, and submission in relation thereto, that the Indictment and Particulars did not delineate the relevant market, alleging that strong monopoly elements could not endure because there were no barriers to entering the market in which the accused operated, but on the contrary that it was very easy to get into this business which was in a much larger market than charged in the Indictment and Particulars, in that (1) the cost to establish a freight forwarding business in Vancouver for this purpose would be modest—of the order of about $2,000; and that (2) it was not necessary to have offices in Toronto and Montreal; and in that (3) the number of persons required to be employed was small in number and that they could be trained within a very short space of time.

These accused by their evidence and submission in relation thereto, also sought to prove that because the substantial part of their fee was a fixed charge, namely, the amount payable to the railway, and that the variable, that is the floor-ceiling within which they could vary prices, was very narrow and in relation to the total charged was minuscule, therefore, whatever they did even by conspiring could not have the necessary criminal element of "undueness" so as to be an offence under either subsection of the Act.

These accused also sought to prove by its economic evidence and submission that the competitive situation in the relevant market in this case was one which an economist would call oligopoly; and that according to the economic theory of oligopoly, even in the absence of an agreement, the long run pricing behaviour would not likely be significantly different than did obtain here; and therefore no offence was committed.

In brief, these accused in evidence and argument submitted that what these accused did, did not result in them obtaining that quantum of market power to enable them to monopolize or tend to monopolize the business in the alleged relevant market, as envisaged by them, in this case; and that in any event, their conduct, employing whatever market power they did have, did not have the necessary criminal element of "undueness" in that they did not have the power to raise prices as they chose or to exclude competition when they desired to do so.

In respect to the Denning incident, the defence of these accused was that it was a perfectly natural and proper thing to do, viz., to eliminate a competitor, and that anything they did in this regard was not illegal.

Counsel for the Crown in submitting argument as to the import of the economic evidence adduced, stated that "it was proper to submit economic evidence to the Court, and that there should be a welding of law and economics

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in combines cases". Crown counsel also agreed and submitted (*a*) that there shoud be no invention of markets, economic gerrymandering of the market, tearing a market out of context, creating a market out of bits and pieces of the whole market, deciding illegality as a prelude to determining the market, all for the purpose of obtaining a conviction; (*b*) that the exclusion of true substitutes is wrong; (*c*) that the exclusion of true competitors is wrong; (*d*) that "unduly" should be considered within the boundaries of the true relevant economic market; (*e*) that in defining the true relevant market in this case that the following characteristics or dimensions should be considered, namely, (i) product substitutability; and (ii) geographical area; and (*f*) that in testing whether the relevant market has been correctly defined, the additional features or indicators of the structural characteristics of such relevant market, of competitors and "poised" competition should also be considered.[8]

So much for the submission of counsel in respect to the Indictment against the accused Mills, Leimar and Kuehne & Nagel (Canada) Limited.

As to these accused, I now deal with the evidence of the competitive features in their collusive aspects, firstly, in relation to market structure, and secondly in relation to behaviour or conduct.

In my view, firstly, there were no substitute services for this service business in which the accused operated, that is to say, the facilities solely by ship and solely by air and the transportation business in connection therewith in relation to articles and commodities transported from the said designated area of the Orient to Toronto and Montreal were and are in another market and not the market in which these accused carried on their businesses.

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[8] In reference to the feature or indicator of "poised" competition, c.f Spence J. in *Regina v. Howard Smith Paper Mills, Limited et al* [1954] O R. 543 at 578:—

> At best it is a fringe type of competition where the lower-priced and coarser products of the accused mills might find some competition from the coarse paper mills and in industry there is always a possibility of substitution if the product becomes substantially too high in price. If the public had to rely on this distant possibility its protection would be slight indeed

Secondly, the barriers of entry to the alleged relevant market were high. Part of the proof of this is the fact that new persons did not get into this market (Mr. Mardock confirmed this (see Exhibits 273,207 and 280)); what happened to Denning is an example; Johnston also was only able to get five per cent of this market; and Freight Consolidators of Canada Limited obtained a negligible amount of this business; Denning experienced "operation clobber" put in effect by Leimar and Mills, which cost it $32,000 in six to seven months in its Vancouver operation; and Mills and Leimar were successful in stopping newcomers to this market to have access to the ships manifests (see Exhibits 265-188).

In this connection also, Leimar and Mills succeeded in preventing the truckers from getting O.C.P. preferential rates (see Exhibits 263-148).

In addition, the problem of getting customers in this market was substantial. Only if you have had some close relationship with importers, as for example, customs brokers, was it possible to enter. That is how Leimar, Mills, Kuehne & Nagel (Canada) Limited and Denning got into this market. But even the FCC Company run by a group of customs brokers has not had much success. And Johnston with all its connection in the trucking business was only able to get about five per cent of the market.

Thirdly, there was really no issue about the geographical market even though it was raised in the evidence.

Fourthly, the evidence established that in relation to this alleged relevant market (*a*) where the buyer of these services required transportation without regard to time, he used water transportation; (*b*) where the buyer required fast transportation he used ship-rail or in some cases trucks; (*c*) that the truckers did not have the benefit of O.C.P. rates; (*d*) that the accused Leimar, Mills and Kuehne & Nagel (Canada) Limited agreed to use all possible measures to exclude trucks and other freight forwarders from the market; (*e*) that the agreement between the accused Leimar, Mills and Kuehne & Nagel (Canada) Limited was to exclude all competitors including truckers; (*f*) that the railways were not real competitors because of Railway Rule 43, among other things; (*g*) that the importers (who could not take advantage of the tariff)

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were not real competitors; (*h*) that the airlines were not real competitors; (*i*) that at the best time, the truckers serviced only 20 per cent of the market; (*j*) that many importers preferred railway transport over truck (door to door) deliveries; (*k*) that all substitutes were imperfect and that the competitors (outside of pool cars) were not true competitors; (*l*) all of the customers of the freight forwarders resided in Ontario and Quebec, mainly in Toronto and Montreal; (*m*) that O.C.P. rates, incidental benefits, and preferential rail rates were available only to persons residing in points east of the Manitoba-Ontario boundary; (*n*) that the combination of transportation by ship and rail provided speedy transit (as compared to water transportation) and economical rates; (*o*) that while water transportation was cheaper than ship-rail transportation, that when speed of delivery was important, that the customer used ship-rail transportation; (*p*) that apart from water transportation that the only substitute for "mixed pool car" was transportation by truck; and (*q*) that apart from very large importers, it was impossible for the average importer to obtain the benefit of the preferential rail rate unless he used the services of a pool car consolidator.

In brief, putting the matter in another perspective, it was established by the evidence that when the Board of Transport Commissioners approved C.F.A. Tariffs (series 70) they created a specific market available to all buyers of the service available therein. Such buyers were all those persons residing in Canada east of the Manitoba-Ontario boundary who wished to import goods from the areas of the Orient designated in these tariffs; and such buyers were entitled to obtain the benefit of these preferential rail tariffs if they were able to consolidate carload shipments of commodities, free of any collusive action by the accused Leimar, Mills and Kuehne & Nagel (Canada) Limited.

For these reasons, and considering the whole of the evidence, I am of opinion that (1) the Indictment and Particulars alleged the true relevant market; and (2) the evidence proved such was the true relevant market in which these accused carried on their respective businesses at the relevant times, beyond a reasonable doubt.

So much for the market structure.

As to the other competitive feature, namely, the behaviour or conduct of the participants in this relevant market, it is clear from the facts recited above from the evidence that the devices employed therein by these accused related to:

(a) prices;

(b) markets or customers;

(c) channels of distribution; and

(d) that the conspiracy, combination, agreement or arrangement restricted persons from entering into or expanding a business in this service industry.

As to any of these, in my view, no dispute can arise from the evidence.

The Crown has proven an agreement or conspiracy by Leimar, Mills, and Kuehne & Nagel (Canada) Limited to fix prices; to divide the markets and customers between themselves; to control the channels of distribution; and to prevent people from entering this service industry; to restrict Denning from entering into or expanding a business in this service industry; and also to restrict Johnston and F.C.C. Company Limited from expanding their business in this service industry.

The fact that there was a ceiling above which it was impossible to raise prices does not affect the question of the behaviour or conduct of these accused in this relevant market (see *Regina v. Northern Electric Co. Ltd. et al*[9]). This is true in every combines case. If the monopoly charges too high a price, the customer will choose, an imperfect substitute as for example, in the case here, water transportation, or will go to the outsider that is, to truckers because the rates are cheaper. Every monopoly is faced by ceilings.

The fact that under the theory of oligopoly prices would have been the same in the long run is irrelevant. No persons are entitled to engage in anti-competitive trade practices or policies because this result may obtain in any event if all things are equal.

The only other question is whether or not such anti-competitive behaviour or conduct of these accused in

[9] [1955] 3 D.L.R. 449 at 476.

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employing the said devices as they did, had the criminal element of "undueness" so as to constitute an offense under section 32(1)(*a*) or section 32(1)(*c*) or both.

The Crown has proven, as stated, that Leimar, Mills and Kuehne & Nagel (Canada) Limited were able to do what they did by obtaining sufficient market power by their said agreements and conspiracy in relation to this service business in this said relevant market.

The Crown has proven also that the object of these accused at all material times was twofold, namely, (1) to limit the facilities for transporting or dealing in the said articles or commodities that may be the subject of trade or commerce, and also (2) the prevention or lessening of competition in the transportation of such articles or commodities also, in such relevant market.

The success of these accused in interfering with "free competition" in this service business in this relevant market at all material times was most substantial. For this reason and also because of the gross predatory practices engaged in by these accused, above mentioned, the conclusion is inescapable that the conduct and behaviour of these accused in relation to "free competition" at the material times in relation to both Count 1 and Count 2 of the Indictment, had the inordinate quantum against the public interest so as to be "unduly" beyond a reasonable doubt, as that word is judicially meant in the cases, and within the meaning and import of that word as employed in both section 32(1)(*a*) and section 32(1)(*c*) of the *Combines Investigation Act*.

The verdict of the Court therefore is that the accused Overland Import Agencies Ltd. (Leimar Forwarding Co.), J. W. Mills & Son Limited and Kuehne & Nagel (Canada) Limited are guilty on both Count 1 and Count 2 of the Indictment herein.

SCHEDULE "A" to
REASONS FOR JUDGMENT

IN THE EXCHEQUER COURT OF CANADA

HER MAJESTY THE QUEEN

against

J. W. Mills & Son, Limited (sometimes known as J. W. Mills & Son, Ltd. and as J. W. Mills & Son Limited)

Kuehne & Nagel (Canada) Limited (sometimes known as Kuehne & Nagel (Canada) Ltd.)

Overland Import Agencies Ltd. (formerly known as Mardock Enterprises Ltd)

Denning Freight Forwarders Ltd.

Johnston Terminals Limited

J. W. Mills & Son, Limited (sometimes known as J. W. Mills & Son, Ltd. and as J. W. Mills & Son Limited)

Kuehne & Nagel (Canada) Limited (sometimes known as Kuehne & Nagel (Canada) Ltd)

Overland Import Agencies Ltd. (formerly known as Mardock Enterprises Ltd.).

Denning Freight Forwarders Ltd.

Johnston Terminals Limited

stand charged

1. That between the first day of January, 1956, and the first day of August, 1966, both inclusive, within the Province of British Columbia, did unlawfully conspire, combine, agree or arrange together and with one another and with

Leithdyke Forwarders Limited (sometimes known as Leithdyke Forwarders Ltd.)

Thomas Meadows & Company Canada, Limited

Leith Services Ltd., and Mardock Enterprises Ltd. (formerly carrying on business under the firm name and style of Leimar Forwarding Co.)

Muirhead Forwarding Limited

Ian F. Mardock (formerly known as Ian F. Gee) the late R. Stanley Leith.

or with some or one of them to limit unduly the facilities for transporting or dealing in articles or commodities that may be the subject of trade or commerce, to wit, articles or commodities, imported from designated areas in the orient into the Province of British Columbia and *which could be* transported by railway in railway cars, the railway cars each ordinarily containing a pool shipment of two or more different kinds of the said articles or commodities, at east bound import freight rates, to points in Canada, east of the Manitoba-Ontario boundary, to the City of Toronto and elsewhere in the Province of Ontario and to the City of Montreal and elsewhere in the Province of Quebec and did thereby commit an indictable offence contrary to section 32(1)(*a*) of the Combines Investigation Act.

2. That between the first day of January, 1956, and the first day of August, 1966, both inclusive, within the Province of British Columbia, did unlawfully conspire, combine, agree or arrange together and with one another and with

Leithdyke Forwarders Limited (sometimes known as Leithdyke Forwarders Ltd.)

Thomas Meadows & Company, Limited

Leith Services Ltd, and Mardock Enterprises Ltd. (formerly carrying on business under the firm name and style of Leimar Forwarding Co.)

Muirhead Forwarding Limited

Ian F. Mardock (formerly known as Ian F. Gee)
the late R. Stanley Leith

or with some or one of them, to prevent, or lessen, unduly, competition in the transportation of articles or commodities that may be the subject of trade or commerce, to wit, articles or commodities imported from designated areas in the orient into the Province of British Columbia and *which could be* transported by railway in railway cars, the railway cars each ordinarily containing a pool shipment of two or more different kinds of the said articles or commodities at east bound import freight rates, to points in Canada, east of the Manitoba-Ontario boundary, to the City of Toronto, and elsewhere in the Province of Ontario, and to the City of Montreal and elsewhere in the Province of Quebec and did thereby commit an indictable offence contrary to section 32(1)(*c*) of the Combines Investigation Act.

Dated this 6th day of
November, 1967, at
Vancouver, Province of
British Columbia.

"R. P. ANDERSON"
Agent of the Attorney General of Canada.

IN THE EXCHEQUER COURT OF CANADA

HER MAJESTY THE QUEEN

against

J. W. MILLS & SON, LIMITED
KUEHNE & NAGEL (CANADA) LIMITED
OVERLAND IMPORT AGENCIES LTD.
DENNING FREIGHT FORWARDERS LTD.
JOHNSTON TERMINALS LIMITED

ADDITION TO PARTICULARS

WITH REFERENCE TO THE PARTICULARS OF THE INDICTMENT, DATED NOVEMBER 6, 1967, THE CROWN FURTHER STATES:

3. (A). IT is not alleged that JOHNSTON TERMINALS LIMITED committed any of the specific aforementioned overt acts, save and except with regard to Paragraph 2 (*a*) (*b*) (*c*) and (*e*) of the said Particulars.

DATED at the City of Vancouver, in the Province of British Columbia, this 6th day of November, A.D. 1967.

"R. P. ANDERSON"
AGENT OF THE ATTORNEY GENERAL OF CANADA

To: The Exchequer Court of Canada
And to· R. M. Hayman, Esq.,
And to· J G Alley, Esq
And to: B D. Kenny, Esq.
And to G S. Cumming, Esq.

These PARTICULARS are furnished by R. P. Anderson Esq, Agent of the Attorney General of Canada, whose place of business and address for service is Suite 220, 890 West Pender Street, Vancouver 1, B.C.

IN THE EXCHEQUER COURT OF CANADA

HER MAJESTY THE QUEEN

against

J W. MILLS & SON, LIMITED
KUEHNE & NAGEL (CANADA) LIMITED
OVERLAND IMPORT AGENCIES LTD.
DENNING FREIGHT FORWARDERS LTD.
JOHNSTON TERMINALS LIMITED

PARTICULARS

WITH REFERENCE TO THE PARTICULARS OF THE INDICTMENT, THE CROWN STATES.

1. THE fundamental ingredients of the alleged (i) conspiracy (ii) combination (iii) agreement or (iv) arrangement are the facts that will be proved by the Crown as constituting the offences charged in the indictment. These offences consist of collusion amongst the accused and co-conspirators to limit unduly the facilities for transporting or dealing in articles or commodities and to lessen unduly competition in the transportation of the said articles or commodities, all of which are subjects of trade or commerce and are imported from a designated geographical area, and include, inter alia, glassware, baskets, artificial flowers, furniture, footwear, groceries, clothing, rugs, musical instruments, imitation jewellery, electrical appliances, sporting goods, toys, optical goods, cutlery and woodenware, such list not being limitative, a complete list of the said articles or commodities being listed, inter alia, in the following Canadian Freight Association Eastbound Import Freight Tariffs and in the supplements and amendments thereto:

(a) Canadian Freight Association #70A—effective July 11, 1951;

(b) Canadian Freight Association #70B—effective June 23, 1961;

(c) Canadian Freight Association #70C—effective May 29, 1963;

all such Tariffs having been issued by the authorized Agent of the Canadian Freight Association, such an Association consisting, inter alia, of all railways with termini in Canada, which Canadian Freight Association Tariffs stipulate, inter alia, the unit price for minimum mixed carload weights of specified articles or commodities, at which certain designated carriers, including the Canadian Pacific Railways and the Canadian National Railways, may carry the said articles or commodities, all of which originated in a designated geographical area, as described in the said Tariffs and land by vessel in the Port of Vancouver, in the Province of British Columbia, and are carried by rail from the said Port to points in Canada in the Provinces of Ontario and Quebec, such points being east of the Saskatchewan-Manitoba Boundary, copies of the said Tariffs and supplements and amendments thereto having been supplied to counsel for the accused.

2. THE alleged (i) conspiracy (ii) combination (iii) agreement or (iv) arrangement is a continuing one during the period between the first day of January, 1956 and the first day of August, 1966, the said (i) conspiracy (ii) combination (iii) agreement or (iv) arrangement being manifested, inter alia, by the following overt acts of the accused or the co-conspirators, or some of them, or their agents, in furtherance of the said (i) conspiracy (ii) combination (iii) agreement or (iv) arrangement:

(*a*) Preparing, writing, signing and sending letters, telegrams, memoranda, rate-sheets, schedules of customers or consignees (hereinafter known as "consignees") or other documents to one another or to some other participants, or to other persons and the said documents, without limiting the foregoing, are more particularly identified and set forth as those being seized in:

VANCOUVER—by the authorized representatives of the Director of Investigation and Research, appointed under the Combines Investigation Act, R S C 1952, Chapter 314 at 340 Burrard Street, Vancouver, B C on or about January 31, 1961 and by the R.C.M. Police at 1045 Pender, Vancouver, B C on or about June 23, 1966;

TORONTO—by the authorized representatives of the Director of Investigation and Research, appointed under the Investigation Act, R S C 1952, Chapter 314, at 159 Bay Street, Toronto, Ontario, on or about February 2, 1961 and, by the R C M. Police at 159 Bay Street, Toronto, Ontario, on or about June 23, 1966;

MONTREAL—by the authorized representatives of the Director of Investigation and Research, appointed under the Combines Investigation Act, R S C Chapter 314, at 485 McGill Street, Montreal, P Q. on or about February 2, 1961 and by the R C.M. Police at 485 McGill Street, Montreal, P Q on or about June 22, 1966;

VANCOUVER—by the authorized representatives of the Director of Investigation and Research, appointed under the Combines Investigation Act, R S C 1952, Chapter 314, at 1035 West Pender Street, Vancouver, B C, on or about February 2, 1961 and August 4, 1961, and by the R C M. Police at 1035 West Pender Street, Vancouver, B C, on or about June 24, 1966;

MONTREAL—by the authorized representatives of the Director of Investigation and Research, appointed under the Combines Investigation Act, R S C. 1952, Chapter 314, at 407 McGill Street, Montreal, P Q, on or about January 31, 1961, and by the R.C M. Police at 407 McGill Street, Montreal, P Q., on or about June 23, 1966;

VANCOUVER—by the authorized representatives of the Director of Investigation and Research, appointed under the Combines Investigation Act, R.S C. 1952, Chapter 314, at 2020 Yukon Street, Vancouver, B.C, on or about February 9, 1961, and by the R C.M. Police on premises used or occupied by the said accused at 2020 Yukon Street, Vancouver, B C, on or about June 23, 1966;

TORONTO—by the authorized representatives of the Director of Investigation and Research, appointed under the Combines Investigation Act, R.S C. 1952, Chapter 314, at 200 Bay Street, Toronto, Ontario, on or about February 3, 1961, and by the R.C.M. Police at 200 Bay Street, Toronto, Ontario, on or about June 28, 1966;

MONTREAL—by the authorized representatives of the Director of Investigation and Research, appointed under the Combines Investigation Act, R S C. 1952, Chapter 314, at 759 Victoria Square, Montreal, P.Q., on or about June 27, 1966;

TORONTO—by the authorized representatives of the Director of Investigation and Research, appointed under the Combines Investigation Act, R.S C. 1952, Chapter 314, at 185 Bay Street, Toronto, Ontario, on or about March 17, 1961, and by the R C M. Police at 185 Bay Street, Toronto, Ontario, on or about June 28, 1966;

MONTREAL—by the authorized representatives of the Director of Investigation and Research, appointed under the Combines Investigation Act, R S C. 1952, Chapter 314, at 759 Victoria Square, Montreal, P Q, on or about June 27, 1966;

TORONTO—by the authorized representatives of the Director of Investigation and Research, appointed under the Combines Investigation Act, R S.C. 1952, Chapter 314, at 185 Bay Street, Toronto, Ontario, on or about March 17, 1961, and by the R.C.M. Police at 185 Bay Street, Toronto, Ontario, on or about June 28, 1966;

MONTREAL—by the R C M Police at 1155 Dorchester Blvd West, Montreal, P Q, on or about October 12, 1966, and at the C N R. Turcott Yards, Montreal, P Q, on or about October 13, 1966;

copies of all the said documents having been supplied to counsel for all the accused.

(*b*) Having, keeping, or retaining in their possession or in the possession of their agents, or on their premises, or on premises used or occupied by them, the said letters, telegrams, memoranda, rate sheets, schedules of consignees or other documents received or obtained from another accused or other accused or another co-conspirator or other co-conspirators, or some of them or their agents, as cited in paragraph 2(*a*) above;

(*c*) Arranging to publish similar or identical rates, which rates were to be charged to their consignees;

(*d*) Arranging to assess similar or identical charges to consignees or their agents for a certain category or type of information or advice sent via their communication facilities in the Port of Vancouver to the said Cities of Toronto and Montreal and to provide, free of charge, to the said consignees or their agents another category or type of information and advice sent via the said communication facilities from the said Port of Vancouver to the said Cities,

(*e*) One of the accused agreeing with a co-conspirator that the former would not solicit, or attempt to solicit, any import business relating to articles or commodities imported from the said designated geographical area to the said Port of Vancouver for carriage by railway pool car from the said Port to the said Cities, in return for which the latter would not solicit or attempt to solicit any domestic traffic for carriage by railway pool car from the said Port to the said Cities;

(*f*) Arranging, by certain written agreements which provided, inter alia, that there would be no reduction of rates, or varying or cancellation of terms, or soliciting of listed consignees, without prior notice being given to, and the concurrence of, the other parties to the said document or documents, all such documents being contained among those cited in 2(*a*) above;

(*g*) Arranging for, participating in, or attending meetings or conferences, for the purpose of attempting to persuade persons and agents of shipping companies or shipping lines, located in the Port of Vancouver, to refuse access of certain documents to a competitor, which documents related to the said imported articles or commodities being carried from the Port of Vancouver to the said Cities;

(*h*) Issuing rate sheets and terms to their consignees, which rate sheets and terms became effective at similar times, the said rates usually being below the normal rates normally charged by them to the said consignees, all with the prime object of forcing another competitor from the import pool car business with regard to articles being carried from the Port of Vancouver to the said Cities;

(*i*) Two of the accused agreeing with a co-conspirator that the latter would represent them in some of the negotiations with another accused with regard, inter alia, to the cessation of a rate war and the withdrawal by the latter said accused from the import pool car traffic originating in the Port of Vancouver and terminating in the said Cities;

(*j*) Three of the accused agreeing with a co-conspirator that one of the accused would withdraw all of its facilities from the Port of Vancouver, in the implementation of one of the terms stipulated in certain written agreements;

(*k*) Arranging to utilize certain non-competitive solicitation methods concerning consignees;

(*l*) Arranging to furnish, or furnishing each other or exchanging with each other, lists of consignees, which consignees had been solicited by another of the accused, a co-conspirator or some of them or their agents;

(*m*) The payment by three of the accused to another accused of monthly commissions for the exclusive right to solicit the latter's former consignees which consignees had, by agreements, been allocated by one of the accused to three of the said accused,

3. (A) ALL of the accused, together with some of the co-conspirators or their agents, were engaged in the business of railway pool car consolidations of the said articles or commodities and the facilities, functions and methods carried out or used by them in the operation of the said business were essential to, and formed an integral part of, the said transportation by rail as described in paragraph 1, herein.

(B) THE facilities were offices, equipment and furnishings and those railway pool car consolidation functions and methods, carried out or used by the accused, together with some of the co-conspirators or their agents, concerned with or relating to the said articles or commodities imported by vessel from the said geographical area and transported by rail pool car from the Port of Vancouver to the said points, all of which functions and methods are within the knowledge of the accused and the co-conspirators, and consist, inter alia, of

(*a*) All of the offices, staff, equipment and furnishings of the accused corporations and their agents, in the Cities of Vancouver, Toronto and Montreal, including communication facilities owned or rented, which facilities were frequently utilized for rapid communication of certain information and advice from the Port of Vancouver to the Cities of Toronto and Montreal and from the Cities of Toronto and Montreal to the Port of Vancouver.

(*b*) Arranging for the consolidation of the said articles or commodities, in order to obtain the benefit of the said tariffs, inter alia;

(*c*) Advising the consignee in advance of the approximate date of arrival in the Port of Vancouver by steamship of the said articles or commodities;

(*d*) Obtaining information from a steamship company or line or their agents regarding the said articles or commodities, all such information normally being listed in the steamship manifest of the said vessel;

(*e*) Arranging for the release of the said articles or commodities from the steamship company or vessel agent;

(*f*) Preparing the necessary documentation for the immediate loading and carriage of the said articles or commodities by railway pool car, the railway pool cars normally consisting of a consolidation of two or more of the said imported articles or commodities;

(*g*) Preparing and transmitting the necessary instructions and details to the dock operators in the Port of Vancouver, or their agents, concerning the loading, handling, nature and mode of carriage of the said articles or commodities,

(*h*) Delivering, by means of their own employees inter alia, written instructions to the Canadian Pacific Railways or the Canadian National Railways, or their agents, regarding the number of pool cars that the said railway Companies should immediately dispatch to a particular dock or shed area, in the said Port of Vancouver, for the purpose of loading certain pool car consolidations, consisting of the said articles or commodities, into the said railway pool cars;

(*i*) Instructing the said railway Companies, or their agents, concerning any particular temperature conditions or other specific precautions or measures that should be taken by them with regard to the preservation or safety of particular articles or commodities being carried in a railway pool car from the said Port of Vancouver to the said Cities;

(*j*) Preparing the necessary documentation, required, inter alia, by Canadian Customs, to facilitate the rapid and efficient dispatch of the said articles or commodities, via railway pool cars from the said Port to the said Cities;

(*k*) Obtaining from the said railway Companies, following the loading of the said pool cars, information regarding the car numbers and the way bill numbers for the noting of the same on the invoice normally forwarded by the accused or co-conspirator to particular consignees, which invoice includes in one charge, inter alia, (1) the freight due to the said railway Companies by a consignee and (2) the pool car consolidation fees also due by a consignee,

(*l*) Notifying a particular consignee of the time of departure from the said Port of Vancouver of the said articles or commodities by railway pool car and the expected date of arrival at the ultimate railway destination;

(*m*) Advising the consignee of any ocean freight, or other charges, which may be due to the vessel which transported the said articles or commodities to the said Port of Vancouver;

(*n*) Advising the consignee of any shortages or damages in the said articles or commodities and, if necessary, attempting to trace the location of any articles or commodities and placing damage claims or reports with the suitable authorities or their agents, (*o*) Assuming the responsibilities of, and acting as, a shipper, vis-a-vis the said Canadian Pacific Railways and Canadian National Railways, with regard to the articles or commodities carried from the said Port of Vancouver to the said Cities;

It is not alleged that the accused corporations own or control the physical means of carriage, the physical means of carriage from the Port of Vancouver being, in every case, provided by, and, to the Crown's knowledge, owned by, the said Canadian National Railways and the Canadian Pacific Railways.

(C) THE facilities referred to, or some of them, were located at all those points at which the accused, together with some of the co-conspirators or their agents, carried out or performed the said pool car consolidation functions and methods;

(D) THE conspiracy, combination, agreement or arrangement is to be inferred from all the evidence which will be adduced by the Crown. Detailed particulars of many of the acts and declarations cannot be given without setting out all of the evidence upon which the Crown will rely but the important overt acts which illustrate the nature and extent of the limiting of facilities and the preventing or lessening of competition are set out herein

DATED at the City of Vancouver, in the Province of British Columbia, this 6th day of November, A D. 1967.

"R. P. ANDERSON"
AGENT OF THE ATTORNEY GENERAL OF CANADA

To· The Exchequer Court of Canada
And To: R. M. Hayman, Esq.
And To: J. G. Alley, Esq.
And To: B. D. Kenny, Esq.
And To G. S. Cumming, Esq

These PARTICULARS are furnished by R. P. Anderson, Esq., Agent of the Attorney General of Canada, whose place of business and address for service is Suite 220, 890 West Pender Street, Vancouver 1, B C.

SCHEDULE "B" to
REASONS FOR JUDGMENT

"RELEVANT MARKETS" IN CANADIAN COMBINES CASES DEFINED IN TERMS OF "COMMODITY" AND "GEOGRAPHY"

	Commodity	*Geography*
R v Master Plumbers et al (1907) 14 O.L R. 295	Plumbing Supplies	Province of Ontario
R v. Hobbs Glass Ltd. et al [1950] S C. of Ont.	Glass	Provinces of Ontario and Quebec
R v. McGavin Bakeries Limited et al (No. 6) (1951) 3 W.W.R. 289	Bread and Bakery Products	Provinces of British Columbia, Alberta and Saskatchewan
R v. Goodyear Tire & Rubber Co. of Canada Ltd. et al (1954) 108 C C C 321	Rubber Products	Canada
R v. Howard Smith Paper Mills Limited et al [1954] 4 D L R. 161	Fine Papers	Provinces of Ontario and Quebec
R v. Crown Zellerbach Canada Ltd. et al (1955) 14 W W.R. 433	Coarse Papers	Province of British Columbia
R v Dominion Steel and Coal Corporation Ltd. et al (1957) 116 C.C C. 117	Steel Wire Fencing and related products	City of Toronto and City of Montreal
R v. D. E. Adams Coal Ltd et al (1957) 23 W.W R. 419	Coal	City of Winnipeg
R v Gair Company of Canada Limited (1958) Trial, Quebec Court of Queen's Bench	Paperboard Products	City of Montreal and elsewhere in Canada east of the Province of Saskatchewan
R v. Lyons Fuel Hardware and Supplies Limited et al (1961) 131 C.C C. 189	Coal	City of Sault Ste. Marie
R v. Electrical Contractors Association of Ontario and Dent (1960) 127 C C C. 273 (Trial)	Electrical Construction Materials and Equipment	Province of Ontario
R v. St. Lawrence Corporation Limited et al (1966) Trial Supreme Court of Ontario (unreported)	Corrugated Box Containers	Toronto and elsewhere in Canada
R v. Stinson-Reeb Supply Co, Ltd et al (1929) 52 C C C. 66	Gypsum Products	City of Montreal

SCHEDULE "C" to
REASONS FOR JUDGMENT

Public Policies Toward Business Third Edition 1966, p. 156 by Clair Wilcox, Ph D.

The Line of Commerce

To determine a relevant market, a court may find it necessary to define the commodity with which it is concerned. This problem does not arise with products such as cigarettes and shoe machinery. But where a product has close substitutes, the court must decide whether to exclude or include them when it measures market power. If substitution were to be ignored, every brand would have a monopoly. If all possible substitutes were to be taken into account, monopoly would be rare indeed The question is where to draw the line

Like products may have different physical characteristics; they may have different end uses; they may sell in different price lines; their markets, therefore, may be distinct. *Like products,* on the other hand, *may be readily interchangeable; their market, therefore, will be the same* The degree of interchangeability is to be measured by cross-elasticity of demand. Cross-elasticity defines the extent to which a change in the price of one product affects the sales of another If a slight change in the price of product A results in a large change in the sales of product B, cross-elasticity is high. Conversely, if a sharp change in the price of A has little effect on sales of B, cross-elasticity is low In the first case, substitution occurs so readily that the two products can be held to occupy a single market In the second, the possibility of substitution is so remote that the markets for the two must be regarded as separate.

Competition and the Law, p 42 by Sumner Marcus, (quoting in part from *U S. v. Continental Can. Co. et al* case).

. . . the Court . . chooses . . . to invent a line of commerce the existence of which no one, not even the government, has imagined; for which businessmen and economists will look in vain; a line of commerce which sprang into existence only when the merger took place and will cease to exist when the merger is undone.

Other critics of these two decisions have accused the Court of "economic gerrymandering".

Competition and Monopoly—Legal and Economic Issues, p. 453, footnote 211, by Mark S Massel.

"The market, then, does not perform the function of a rule of law. It operates, rather, to orient, systematize and classify factual situations so that anti-trust policies can be properly applied *As a tool of factual analysis, the market concept should not be a draw-string, which is tightened for illegality* and slackened for lawfulness. To attain the clarity of thought necessary for intelligent policy formulation and the rudiments of predictability essential to the administration of this body of law, the concept of the market should remain a constant" Note, "The Market· A Concept in Anti-trust," *Columbia Law Review,* Vol. 54 (1954), pp. 580, 603.

Antitrust Policy—An Economic and Legal Analysis (1959), p. 134 by Carl Kaysen and Donald F. Turner

. . . *Without a minimally reasonable definition of markets, criteria based on quantitative shares become whimsy*

Stanford Law Review—Oligopoly Power, p. 306 by Bradley

> . . . Indeed, the conclusion seems inescapable that in *Alcoa-Rome* and *Continental Can the market definition was not so much the prelude to the conclusion of illegality as the conclusion of illegality was the prelude to the market definition.*

United States v. Grinnell Corporation et al (U S. S.C.R. 16 L ed 2d) p. 795

> In section 2 cases, *the search for "the relevant market" must be undertaken and pursued with relentless clarity. It is, in essence, an economic task put to the uses of the law.* Unless this task is well done, the results will be distorted in terms of the conclusion as to whether the law has been violated and what the decree should contain.

page 798

> *The gerrymandered market definition approved today* totally excludes from the market consideration of the availability in Pittsburgh of cheaper but somewhat less reliable local alarm systems, or of more *expensive* (although the expense is reduced by greater insurance discounts) *watchman service,* or even of unaccredited central station service which virtually duplicates the Holmes service.
>
> Instead, and in the name of "commercial realities", we are instructed that the "relevant market"—which
>
> *(384 US 592)
>
> totally *excludes these locally available alternatives—requires us to look only to accredited central station service, and that we are to include in the "market" central stations which do not furnish burglary protection and even those which serve such places as Boston and Honolulu.

United States v. Continental Can Co. et al (378 US 441, 12 L ed 2d 953, 84 S Ct 1738) p. 975

> In any event, *the Court* does not take this tack. *It chooses instead to invent a line of commerce the existence of which no one, not even the Government, has imagined; for which businessmen and economists will look in vain; a line of commerce which sprang into existence only when the merger took place and will cease to exist when the*
>
> *(378 US 477)
>
> **merger is undone.*

Vancouver 1968 Mar. 19-21 Ottawa Apr. 4

BRITISH COLUMBIA ADMIRALTY DISTRICT

BETWEEN:

SOCIEDAD TRANSOCEANICA CANOPUS S.A., OWNERS OF THE VESSEL M.S. *PROCYON* .... PLAINTIFF;

AND

NATIONAL HARBOURS BOARD ....DEFENDANT.

Crown—Shipping—National Harbours Board Act, R.S.C. 1952, c. 187, s. 39—Displaced mooring buoy in Vancouver Harbour—Whether duty of Harbour Board to warn ships—Collision—Whether negligence—Liability of Board for negligence of servants and agents—Limitation of actions—Action against Crown for negligence of servant—Statute of Limitations, R.S.C. 1952, c. 370, s. 11(2).

The M.S. *Procyon* suffered damage to her propeller on the night of November 22nd 1959 in Vancouver Harbour when she collided with a mooring buoy which as defendant Board's officers knew had some weeks earlier been displaced by a storm from her charted location to a position away from shipping channels, and the day before the accident had again been shifted away from shipping channels by floating logs; but defendant's officers did not know that the buoy had again been displaced shortly before the collision to a position where it was a hazard to navigation. The ship's owner sued defendant Board on the Admiralty side claiming damages under s. 39 of the *National Harbours Board Act* by reason of the negligence of defendant, its servants or agents in failing to give warning of the displaced buoy.

Held, dismissing the action, if a proper lookout had been kept as it should have been whilst the ship was navigating Vancouver Harbour at night the lookout should have observed the buoy and warned the ship's pilot of its position, and the accident would have been avoided.

Held also, the effect of s. 39 of the *National Harbours Board Act* is to make the liability of the Crown for the negligence of officers and servants of the Board enforceable by action against the Board in a court having jurisdiction between subjects (*Smith v. C.B.C.* [1953] O.W.N. 212; *Formea Chemicals Ltd v. Polymer Corp.* [1967] 1 O.R. 546; *Langlois v. Can. Commercial Corp.* [1956] S.C.R. 954, referred to); but such an action can only succeed against the Board if it would have succeeded against an officer or servant of the Board. (*The King v. Anthony* [1946] S.C.R. 569 referred to).

Semble: The limitation period of 12 months fixed by s. 11(2) of the *Statute of Limitations* for commencing an action against a person for an act, neglect or default, &c, does not apply to a claim against the Crown (or, as in this case, its statutory agent) in respect of the negligence of its servant.

ACTION FOR DAMAGES.

J. R. Cunningham for plaintiff.

N. D. Mullins and *L. T. R. Salley* for defendant.

JACKETT P.:—This is an action instituted in the Registry for the British Columbia Admiralty District for damages sustained by the Motor Ship *Procyon* when it came in contact with a mooring buoy in Vancouver Harbour on November 13, 1962.

The defendant is a corporation constituted by the *National Harbours Board Act,* R.S.C. 1952, c. 187, and is, for all purposes of that Act, the agent of Her Majesty in right of Canada (s. 3(2)) and, as such, has jurisdiction over Vancouver Harbour (s. 6). It has, as agent for Her Majesty, administration, management and control of property vested in Her Majesty, but has not, ordinarily, any jurisdiction over private property or rights (s. 7). It follows, from its status as an agent of Her Majesty, that, when it employs an officer, clerk or employee, as it is authorized to do by s. 4, the officer, clerk or employee becomes an officer of Her Majesty.[1] Nevertheless, in certain circumstances, claims for torts committed by such persons in the course of their employment may be enforced by actions brought by proceedings against the National Harbours Board. See s. 39, which reads as follows:

> 39.(1) Subject as hereinafter provided any claim against the Board arising out of any contract entered into in respect of its undertaking or any claim arising out of any death or injury to the person or to property resulting from the negligence of any officer or servant of the Board while acting within the scope of his duties or employment may be sued for and prosecuted by action, suit or other proceeding in any court having jurisdiction for like claims between subjects.

The language of s. 39 is to be compared with the language of s. 19(*c*) of the *Exchequer Court Act,* R.S.C. 1927,

[1] The defendant is a statutory corporation that has no existence except for the purposes of the *National Harbours Board Act.* By s. 3(2) it is, for all purposes of that Act, an agent of Her Majesty. It follows that, when it exercises the power conferred on it by s. 4 to employ officers, clerks and employees, it does so in its capacity as agent of Her Majesty, and the persons so employed therefore become officers, clerks or employees of Her Majesty. See *National Harbours Bd. v. Workmen's Compensation Com'n,* (1937) 63 Que. K.B. 388 (per Barclay J. at pages 391-2).

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c. 34, being the version of that Act in force when the *National Harbours Board Act* was enacted by c. 42 of the Statutes of 1936. Sec. 19(*c*) then read as follows:

> 19. The Exchequer Court shall also have exclusive original jurisdiction to hear and determine the following matters:
>
> * * *
>
> (*c*) Every claim against the Crown arising out of any death or injury to the person or to property resulting from the negligence of any officer or servant of the Crown while acting within the scope of his duties or employment upon any public work.[2]

It had long been established that s. 19(*c*) made the Crown in right of Canada liable for the "negligence" of its officers or servants acting in the course of their employment notwithstanding that it was, in terms, a provision that dealt only with the jurisdiction of the Court.[3] Sec. 39, which, in terms, refers to a claim arising out of death or injury resulting from "negligence of any officer or servant of the Board while acting within the scope of his duties or employment", as has already been indicated, must be referring to such a claim based upon negligence of an officer or servant of Her Majesty who has been employed by the Board in its capacity as agent of Her Majesty because there cannot legally be anybody else who can be described as an "officer or servant of the Board". What s. 39 does, therefore, is to make such liability of Her Majesty, in the case of the negligence of that limited class of employees, enforceable by action brought against the Board in a court having jurisdiction between subjects.[4]

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[2] This paragraph was re-enacted in 1938 with the omission of the concluding words "upon any public work" by c. 28 of the statutes of that year.

[3] *The King v. Armstrong,* (1908) 40 S.C.R. 229; *The King v. Desrosiers,* (1909) 41 S C R. 71; *The King v. Murphy,* [1948] S.C.R. 357.

[4] From this point of view, in my opinion, s. 39, while not as explicit, has the same effect (i.e., the effect of making it possible to enforce a liability of Her Majesty by suing the statutory agent) as s. 4 of the *Canadian Broadcasting Act,* c. 24 of the Statutes of 1936, as amended by c. 51 of the Statutes of 1950, which read in part:

> "(2) The Corporation is for all purposes of this Act an agent of His Majesty and its powers under this Act may be exercised only as agent of His Majesty.
>
> (3) Actions, suits or other legal proceedings in respect of any right or obligation acquired or incurred by the Corporation on behalf of His Majesty, whether in its name or in the name of His Majesty, may be
>
> (*a*) brought or taken against the Corporation . . . , or

Since the *National Harbours Board Act* was first enacted in 1936, Parliament has extended the liability of the Crown for torts by the enactment of the *Crown Liability Act* (c. 30 of the Statutes of 1952-3), s. 3(1) of which reads as follows:

> 3.(1) The Crown is liable in tort for the damages for which, if it were a private person of full age and capacity, it would be liable
>
> (*a*) in respect of a tort committed by a servant of the Crown, or
>
> (*b*) in respect of a breach of duty attaching to the ownership, occupation, possession or control of property.

These provisions must be read with s. 7(1), s. 8(1) and (2), and s. 23 of the *Crown Liability Act*, which read as follows:

> 7 (1) Except as provided in section 8, and subject to section 23, the Exchequer Court of Canada has exclusive original jurisdiction to hear and determine every claim for damages under this Act.
>
> * * *
>
> 8 (1) In this section "provincial court" with respect to any province in which a claim sought to be enforced under this Part arises, means the county or district court that would have jurisdiction if the claim were against a private person of full age and capacity, or, if there is no such county or district court in the province or the county or district court in the province does not have such jurisdiction, means the superior court of the province.
>
> (2) Notwithstanding the *Exchequer Court Act*, a claim against the Crown for a sum not exceeding one thousand dollars arising out of any death or injury to the person or to property resulting from the negligence of a servant of the Crown while acting within the scope of his duties or employment may be heard and determined by the provincial court, and an appeal lies from the judgment of a provincial court given in any proceedings taken under this section as from a judgment in similar proceedings between subject and subject.

(*b*) brought or taken by the Corporation, in the name of the Corporation in any court that would have jurisdiction if the Corporation were not an agent of His Majesty."

and the similar provisions inserted by c. 51 of 1950 in other Crown Corporation statutes See *Smith v. C.B.C.*, [1953] O.W.N 212, where Judson J held that s. 4 authorized actions against the statutory agent in tort. (See, however, the *obiter dicta* doubt expressed by the majority of the Court of Appeal in *Formea Chemicals Ltd v. Polymer Corp*, [1967] 1 O.R. 546 at 553.) Sec 4 probably does not go as far as s 10 of the *Canadian Commercial Corporation Act,* c 4 of the Statutes of 1946, which provided that that corporation might sue or be sued in respect of any right or obligation acquired or incurred by it on behalf of His Majesty "as if the right or obligation had been acquired or incurred on its own behalf". Compare *Langlois v. Can Commercial Corp*, [1956] S.C.R 954 Sec 10 excluded the application of rules of substance applicable only to the Crown.

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23. Subsection (1) of section 7 and subsections (1) and (2) of section 8 do not apply to or in respect of actions, suits or other legal proceedings in respect of a cause of action coming within section 3 brought or taken in a court other than the Exchequer Court of Canada against an agency of the Crown in accordance with the provisions of any Act of Parliament that authorizes such actions, suits or other legal proceedings to be so brought or taken; but all the remaining provisions of this Act apply to and in respect of such actions, suits or other legal proceedings, subject to the following modifications:

(*a*) any such action, suit or other legal proceeding shall, for the purposes of this Act, be deemed to have been taken in a provincial court under Part II; and

(*b*) any money awarded to any person by a judgment in any such action, suit or other legal proceeding, or the interest thereon allowed by the Minister of Finance under section 18, may be paid out of any funds administered by that agency.[5]

These proceedings were launched against the Board itself in an Admiralty Registry of this court, and were not launched against the Crown by petition of right in the manner contemplated by the *Petition of Right Act*, R.S.C. 1952, c. 210. I was of opinion during the argument, and it was not seriously argued to the contrary, that the plaintiff may recover in these proceedings if, and only if, it brings itself within s. 39 of the *National Harbours Board Act*. If that view is correct, it follows that the plaintiff can only recover if it establishes that the collision in question resulted from "the negligence of any officer or servant of the Board while acting within the scope of his duties or employment". These words are, in effect, the same as those under consideration by the Supreme Court of Canada in *The King v. Anthony*,[6] where it was held that a person claiming against the Crown under the old s. 19(*c*) of the *Exchequer Court Act* had to show that he had a cause of action against the officer or servant of the Crown personally. Compare *Cleveland-Cliffs Steamship Co. v. The Queen*,[7] where the legal

[5] In my view, s. 23 of the *Crown Liability Act* is a statutory recognition that there are other statutory provisions under which the Crown's liability in tort may be enforced by actions brought against statutory agents While other provisions may be more explicit in some ways, they are less explicit than s. 39 of the *National Harbours Board Act* in others. This is one reason for the view that I have already expressed that s. 39 authorizes such an action. Compare *Baton Broadcasting Ltd. v. C.B.C.*, [1966] 2 O.R. 169, and cases cited therein.

[6] [1946] S.C.R. 569.

[7] [1957] S.C.R. 810.

position was being considered in circumstances of the same general character as those arising here.

It must, therefore, be kept in mind when considering the case under s. 39 of the *National Harbours Board Act* that the plaintiff can only succeed if it has pleaded, and established, facts that would have entitled it to judgment against a servant of the Crown employed by the National Harbours Board if the action had been brought against such servant. (It must, of course, also be a cause of action based on things done by that servant in the course of his employment under the *National Harbours Board Act.*)

I do not, therefore, have to consider, as far as s. 39 is concerned, the very difficult question as to whether the Crown would be liable on the facts of this case under s. 3(1)(*b*) of the *Crown Liability Act* for "breach of duty attaching to the ownership, occupation, possession or control of property".

It should also be noted before going into the facts that the case was tried on the basis that, if the plaintiff is otherwise successful, there is to be a reference as to the *quantum* of damages.

The allegations in the statement of claim that bear on the question of liability read as follows:

1. The Plaintiff, of Piraeus, Greece, is the owner of the deep sea merchant vessel, M.S. *Procyon,* of 10,996 gross tonnage, 6,019 net tonnage, approximately 518 feet in length, and 66 feet in breadth, powered by Doxford diesel engines and registered at the Port of Piraeus, Greece.

* * *

3. After dark on November 13th, 1962, the said ship with a duly licensed British Columbia pilot on board, and with a good lookout being kept on board, during her approach to the Burrard Terminals wharf on the north shore of Vancouver Harbour, was struck at the stern by an unlighted steel mooring buoy, which was out of its charted position.

4. The said striking caused damage to the said ship's propeller and her side plates in the way of the aft peak tank.

5. The said striking was occasioned by the negligence of the Defendant, its servants or agents, in the administration, management or control of the said Harbour, in that the Defendant, its servants or agents, knew the said buoy was out of its charted position but in breach of its duty to the Plaintiff failed to notify the said pilot or any person on board the said ship of the fact that the said buoy was out of its charted position, or that it was encumbering the approaches to the said wharf.

6. The Plaintiff claims damages against the Defendant as provided by Section 39 of The National Harbours Board Act R.S.C.

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1952 Chapter 187, for injury to the Plaintiff's property resulting from the negligence of an officer, officers, servant, or servants of the Defendant while acting within the scope of his or their duties or employment.

7. In the alternative, if the said Defendant, its servants or agents were not aware of the said buoy being out of its charted position and encumbering the said approaches, the Defendant, its servants or agents should have known and the Plaintiff says that such lack of knowledge amounted to a failure to properly administer, manage and control the said Harbour, and the Defendant is liable to the Plaintiff by reason of the said failure.

8. Further particulars of the negligence of the Defendant, its servants or agents are as follows:

(a) Failure to replace the said buoy in its stated position after knowledge was received by the Defendant, its servants or agents of its shifting;

(b) Failure to see that the British Columbia Pilotage Authority and the District Marine Agent were notified of the hazard to navigation from the said buoy being out of position and as to its location in the said Harbour;

(c) Failure to see that Notices to Mariners were issued with respect to the said hazard and its location;

(d) Failure to remedy the existence of the hidden danger to navigation by causing the lighting of the said buoy;

(e) Permitting a continuing nuisance in the said Harbour, namely a drifting unmarked buoy, in waters known to be utilized by foreign vessels

* * *

10. The Plaintiff says and will allege at the trial of this action that the said striking and all resultant damages and losses consequent thereon were such that in the ordinary course of things would not have happened under proper administration, management and control of the said Harbour by the Defendant.

It is obvious, as it seems to me, that, having regard to what I have said about a cause of action under s. 39 of the *National Harbours Board Act,* references to the negligence of the defendant, and to the defendant's acts and omissions, are irrelevant and should, as far as s. 39 is concerned, be ignored.[8] On the same basis, it would seem that paragraph 10, which has to do solely with the statutory functions of the defendant, should be ignored as far as a claim based on s. 39 is concerned.

[8] As an agent through whom Her Majesty maintains or administers property, the National Harbours Board is not itself liable by reason of a failure to keep the property safe (*Sanitary Commrs of Gibraltar v. Orfila,* (1890) 15 App. Cas. 400) unless, and to the extent that, there is special legislation providing for claims against the Crown being enforced by action against the Board as a nominated party See *Gilbert Côté et al. v. National Harbours Bd.,* [1959] Rev. Leg. 438, where this principle was applied to the defendant by the Superior Court of Quebec.

I turn now to the facts.

There is no dispute between the parties concerning the collision itself. At approximately 6:44 p.m. on November 13, 1962, the plaintiff's vessel, Motor Ship *Procyon,* suffered damage in Vancouver Harbour from collision with a mooring buoy (hereinafter referred to as "the buoy") belonging to the defendant, which was not in its position as indicated on charts as published by the Canadian Hydrographic Service.

That part of the buoy which was visible above the water when it was in its charted position was cylindrical in shape, 8 feet in diameter, and 3 feet, 6 inches, to 4 feet out of the water. It was painted white on the top and on the sides to within 6 inches from the water line, the 6 inches above the water being painted red. It was made of metal and was anchored, by a 2½ inch chain, 112 feet long, to two concrete "anchor rocks", each of which weighed 12 tons. When the buoy was in 9 fathoms of water, a large part of the chain would lie on the bottom of the harbour.

In 1959, this buoy was placed by the defendant in a part of the harbour (where there were 9 fathoms of water) that had previously been set aside as an area for mooring vessels, as a buoy to which barges could be moored. At that time, there was published in a Department of Transport publication called "Notice to Mariners" (No. 18 of 1959) a notice reading as follows:

BRITISH COLUMBIA

(66) Vancouver Harbour—Off Moodyville—Mooring buoy established.

A red mooring buoy, for use of scows only, has been established in Vancouver Harbour, off Moodyville, in position Latitude 49°18′02″N., Longitude 123°03′36″W.

N. to M. No. 18 (66) 18-2-59.

Authority: District Marine Agent, Department of Transport, Victoria, Canadian Hydrographic Service charts: Nos. 3418 and 3433. Departmental File: No. 7992-41.

The buoy remained in the position so advertised, which was shown on the published charts, until October 13, 1962, when there was a violent storm in the harbour, popularly known as "Hurricane Freda". Following that storm, a survey of the harbour by the Marine Superintendent J. H. Smith, an officer on the defendant's staff, showed that the buoy (sometimes called "the westerly Moodyville buoy")

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"had been dragged out of position", and he so reported to his superior, Captain W. A. Dobie, the Harbour Master. As located just after the storm, the buoy was less than 1,000 feet from its charted position and was not, in the opinion of the Marine Superintendent, who gave evidence in this Court, in its then position, a hazard to navigation. Nevertheless, he anticipated that, in accordance with the ordinary routine of the harbour, the Harbour Master, upon receiving his report, would advise the District Marine Agent of the Department of Transport at Victoria so that mariners would be advised of the changed position of the buoy and steps would be taken to have it moved back to its charted position. In fact, neither the District Marine Agent nor the British Columbia Pilotage Authority were notified, and no steps were taken to have mariners notified of the change in the buoy's position by notices, by radio, or otherwise. Furthermore, the buoy was not, in fact, moved back to its charted position during the period between Hurricane Freda and the collision in question. No explanation was given for these facts and I can only assume that there was a breakdown in ordinary routine.

Nothing is known of any further change in the situation of the buoy until November 12, 1962 when, according to the log of certain officials of the defendant in a post known as the "Signal Bridge", they were informed at 0030 hours (i.e. 12:30 a.m.) by a ship known as the *Colleen L* that twenty-four sections of logs were "adrift E. Moodyville", and that the "West Buoy" (i.e., the buoy in question) had been "caught" and "dragged" to "appro. 200 ft. S.E. Anglo. Can. Mill". The Marine Superintendent, according to his testimony, remembers having been telephoned early that morning concerning the buoy, but does not remember what he was told. He does remember, however, that the information was not such as to indicate that the buoy was, in his judgment a hazard or that any emergency action was required. If, in fact, the buoy was in a position approximately 200 feet from the Anglo-Canadian Mill, it would seem clear that it must have been completely removed from shipping channels and in such shallow water that it was inconceivable that it could be moved anywhere else accidentally. In any event, no action was taken at that time to inform mariners of the position of the buoy, or otherwise to guard against it being a hazard to navigation.

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November 12, the day on which the *Colleen L* reported that the buoy was near the Anglo-Canadian Mill, was, according to Marine Superintendent Smith, a holiday, and nothing was done about the buoy that day. The following day, a patrol boat operated by the defendant, and in charge of Marine Foreman J. B. Smith, went to check on the buoy and found it about 9:00 a.m. that day, November 13, about 400 feet, and not just 200 feet, from the Anglo-Canadian Mill, but still out of harm's way as far as shipping was concerned. (I am inclined to the view that when found by J. B. Smith, the buoy was in the position where it was seen by the *Colleen L.*) So located, it would be in 7 to 8 fathoms of water according to the charts put in evidence. At 3:00 p.m. that afternoon, J. B. Smith again checked the buoy and found it in the same position, which he described as being in a line between the West Indies Dock and the Anglo-Canadian "stiff line", or "standing boom". He so reported to the Marine Superintendent who again concluded that no emergency action was required.

It is common ground that, when the collision occurred at 6:40 p.m. that evening, the buoy was then on the other side of the "stiff line" from where J. B. Smith saw it at 3:00 p.m., and was in a position where it was a hazard to navigation in that it was in waters through which vessels docking at the busy Burrard Terminals Wharf would pass. If J. B. Smith's evidence as to where he saw the buoy at 3:00 p.m. is accepted, and I do accept it, it follows that some time between 3:00 p.m. and 6:40 p.m. that day, the buoy again shifted its position, or it was shifted, this time apparently at least 1,000 feet.

While the buoy was in that position, the *Procyon,* while approaching the Burrard Terminals Wharf in charge of a pilot and without a tug, cleared the end of the Anglo-Canadian "stiff line" to which reference has already been made. At that point her engines were cut. Subsequently, as part of a manoeuvre which had the effect of causing her stern to move to port, her engines were put at dead slow ahead. Immediately thereafter, as her stern moved to port, her propeller came into contact with the buoy with resultant damage, which is the subject matter of this action.[9]

[9] No evidence was given about the damage to "her side plates in the way of the aft peak tank" referred to in the Statement of Claim.

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The pilot did not see the buoy. A lookout had been posted on the bow, but there is no evidence as to whether he, or any other person on board, saw the buoy. If any such person did see the buoy, he did not report it to the pilot.

At the time of the collision, it was dark and overcast. The evidence as to visibility is not very helpful. After the accident, the buoy was quite visible from the Burrard Terminals Wharf. There is no evidence of anybody who actually tried to see the buoy in the position where it was at the time of the accident from the angle at which the *Procyon* was approaching it. The pilot says that it would have been difficult to see it from that angle because of the absence of light from the shore that they were approaching. The Marine Superintendent says that visibility on the water was good in the circumstances then existing. The Marine Foreman says that when in its charted position, the buoy could be seen on a dark night at a distance of 50 feet to 100 feet. In the circumstances, I have found it very difficult to form an opinion as to whether the lookout on the *Procyon* should have seen the buoy (which, as I conceive the accident, must have passed just off the port of the vessel), being probably a dirty white circular object 8 feet in diameter and about 3 feet, 6 inches out of the water. This is a question on which I would have found the assistance of an assessor, or the evidence of a neutral navigator, of assistance. The same remark applies to the problem of deciding whether, had the pilot seen the buoy himself, or been advised of its presence, he would have, or should have, handled the vessel in such a way as to avoid the collision.

Two other difficult questions of a similar character cause me difficulty. First, should the Marine Superintendent Smith, having learned, during the day on November 12, that the buoy had shifted its position once, if not twice, from the position where it was after Hurricane Freda, have anticipated, as a reasonable probability, that it might get shifted again, and this time into a position where it would be a hazard to navigation, and have taken suitable steps at least to warn mariners of its potential danger, if not to have caused it to be removed from the area? Secondly, if the pilot on the *Procyon* had been advised that the buoy was in the position where it was at 3:00 p.m. on that day,

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and that it had been moved there by 24 sections of logs that were adrift, would that warning have caused him to handle his vessel in some way that would have avoided the accident?

I should say that it is quite clear from Marine Superintendent Smith's evidence that he conceived it to be his duty, if he had had reason to apprehend that the buoy was in a position where it was a danger to shipping, to take steps to warn mariners (by advising the pilotage authority, etc., and by radio) and to have the buoy moved out of such position.

If I find the answers to all the questions of fact in favour of the plaintiff, there still remains the question of law as to whether any officer or servant of the Board is himself legally liable to the plaintiff so as to bring into operation s. 39 of the *National Harbours Board Act.*

I propose to come to a conclusion on each of the questions of fact to which I have referred. Before doing so, I should refer to certain other questions that do not cause me equal concern. Counsel for the plaintiff put his case alternatively on certain omissions that he attributed to Captain Dobie, the Harbour Master, but these had to do with Captain Dobie's alleged responsibility for a failure to have mariners notified of the new location of the buoy after Hurricane Freda, and for the buoy not having been put back in its charted position at that time, and, in my view, any such failure cannot be regarded as the cause of the collision that occurred at a different location a month later. I take the same view of any omission by Marine Superintendent Smith to take action after the telephone message to him at 0030 hours on November 12. Assuming, for the sake of argument, that he should have caused an investigation into the situation on November 12, I cannot find that any such investigation should have resulted in any action that would not have been just as timely, as far as the collision in question is concerned, if taken after the investigations that, in fact, took place on November 13.

The only possible fault of any officer or servant of the Board that might conceivably be regarded as the cause of the collision complained of is, in my view, Marine Super-

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intendent Smith's failure to take some action on November 13, when it was established that the buoy had moved a substantial distance from where it was after Hurricane Freda, and that it was located at a place where it was not a hazard to shipping. According to his own testimony, if the buoy had been in a position where it was a hazard to shipping, he should have warned mariners and taken steps to have it removed. However, it was not in such a position. What concerns me is whether, knowing that it had been displaced for a second time, he should have anticipated that this might happen again and have notified shipping of this possibility or taken steps to have it removed. As far as I can tell on the evidence before me, the two known causes of the previous displacements—Hurricane Freda and twenty-four sections of logs being adrift—were sufficiently unusual that it would not have occurred to a reasonably alert and intelligent employee in the Marine Superintendent's position that it was a probability that a further displacement would occur again in the immediate future. Indeed, as far as I can tell, there would have been no more justification for warning mariners of the possibility of this particular buoy becoming a hazard to shipping than there would have been for warning them that any other object in the harbour might be moved by some unforeseen agency so as to become a hazard to shipping. I am confirmed in this conclusion, which I have reached on negative considerations, by the fact that no witness or counsel for either side was able to suggest what force had moved this cumbersome object into the navigation channel between 3:00 p.m. and 6:40 p.m. on November 12, 1962. With reference to the question whether the Marine Superintendent should have taken any steps that he did not take to have the buoy replaced where it belonged, all that I know from the evidence is that it was in fact replaced in its charted position immediately after the collision. As far as I know, this was done as a result of the various responsible officers having done all that could reasonably be expected of them to achieve this result. There is no evidence from which I can conclude that there was anything that Marine Superintendent Smith could have done that would have resulted in the buoy having been replaced

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in its allotted position before the collision occurred. Certainly, no such action was suggested to him during his long and thorough cross-examination.

My conclusion with regard to the question whether a warning of the possibility of the buoy getting into a position where it would be a hazard to navigation would have enabled the ship to avoid the collision is based on the view that no mariner can possibly think that he is entitled to take a ship across a busy harbour such as Vancouver Harbour at night on the assumption that there will be no object on the water of which he must take account. I cannot accept it that any harbour administration must be taken to guarantee such a clear passage any more than any road authority can or does guarantee that there will be no obstructions or hazards to automobile traffic on a highway. As it seems to me, and what evidence there is on the point supports this conclusion, any ship operating in a harbour, no matter what the visibility, must have whatever lookouts are necessary to detect hazards to navigation and must be so navigated as to be able to avoid such hazards when they are detected. If I am correct in that view, as it seems to me, if the pilot had been warned that the buoy might possibly be moved into the proposed path of his ship, he would have put it in the same position in his mind as other possible hazards concerning which he would have to rely on the normal lookouts which would be posted having regard to the visibility and other circumstances. Unassisted by an assessor or by expert evidence, it seems to me to be obvious that a ship is not entitled to navigate in a harbour without keeping a lookout for what is in its path.

Similarly, I have reached the conclusion that the buoy should have been seen by the lookout and was not seen because a proper lookout was not being kept, or, it was seen by the lookout who failed to advise the pilot of its existence. As I conceive the way in which the collision occurred, the buoy must have passed immediately to the port side of the ship and have been much less than 100 feet from a lookout on the bow. If that is so, I cannot imagine that any sort of lookout that would have been of any use to the navigation of the ship could have failed to see an object of the size and

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colouring of the buoy. I am therefore of the view that the lookout was at fault in not having advised the pilot of the buoy hard on the port side.[10]

Had the pilot been advised of the buoy passing close to port, he, as a reasonably prudent pilot, would have realized the danger of a manoeuvre that would result in the stern of the vessel swinging to port and would not have carried out the manoeuvre. In my view, therefore, the cause of the collision was the fault of the ship in leaving the pilot in ignorance of the presence of the buoy. Even if there had been a fault on the part of the harbour personnel in allowing the buoy to be there or in not giving some notice to the pilot concerning the buoy, the effective cause of the collision, in my view, was the failure of the lookout to see the buoy, which he should have seen, and warn the pilot of its presence.

Having regard to my findings of fact, it is unnecessary to reach a conclusion on the very difficult question as to whether Marine Superintendent Smith, or any other member of the defendant's staff, owed any duty to the ship that would give rise to a personal liability by such employee to the ship for a failure to perform one of the duties of his position as an employee of the defendant. If I had to reach a final conclusion on this question, I should have to consider whether the evidence in this case supports a finding of duty such as was made in *Grossman v. The King*.[11] My present view is that there is a difference in principle between the relation of an employee in a harbour to a ship navigating in a harbour, which has a responsibility to take care for its own safe navigation, and the relation of an airport manager to a person being invited to land an aircraft on a runway on which there is a hazard that cannot be seen from the air. I have in mind, of course, the judgment of Kerwin C.J., in *Cleveland-Cliffs Steamship Co. v. The Queen*, where he said:[12]

> There was no duty owing to the appellants on the part of the Dominion Hydrographer to take soundings in the East Entrance

[10] No reference was made in the evidence to the possibility of there having been a lookout at one or more stations on the port side. I should have thought that there should have been such lookouts who should have seen the buoy during the period that this 518 foot vessel must have been passing within a few feet of it while it was moving at a speed of about one knot.

[11] [1952] 1 S.C.R. 571.

[12] [1957] S.C.R. at p. 813.

> Channel and in the circumstances of this case, I am unable to envisage any possible duty to the appellants resting upon any other servant of the Crown, the breach of which could form the basis of a cause of action against him. The case of *Grossman et al. v. The King*, (1952) 1 S C.R. 571, is disinguishable as there Nicholas, the airport maintenance foreman, was held to owe a duty to Grossman.

and the judgment of Rand J. in the same case where he said:[13]

> Nor have there been shown any circumstances that could possibly lead to a cause of action against any servant of the Crown. The administration of navigation aids depends on the action by Parliament in voting money. But apart from that, the conditions under which a Crown servant can be held personally liable to a third person for failure to act in the course of duty to the Crown require that there be intended to be created, as a deduction from the facts, a direct relation between the servant and the third person The primary duty of the Crown servants is to the Crown; and the circumstances in which the servant can, at the same time, come under a duty to a third person are extremely rare The rule laid down in *Grossman v. The King*, [1952] 1 S C.R. 571, is, as I interpret it, this: that the servant from the nature of his specific duty, a duty immediately related to action of the third person, is chargeable with knowledge that the latter, in his own conduct, is justifiably relying on the performance by the servant of that duty, and that the servant is chargeable with accepting the obligation toward the third person. In other words, between them a *de facto* relation of reliance and responsibility is contemplated. There are no such circumstances here. The government administration, as disclosed by the evidence, is of a general character, unrelated directly and immediately to any particular navigational work in these waters and with no acceptance by any of the public servants concerned of obligation toward the third person, nor any immediate reliance on the performance of individual duty related to the latter's use of a public work. Buoys are not warranted fixtures for navigation. Nothing has been shown of neglect in their original placement or of failure to discover their change of position. The "sweeping" and other work suggested to be done in the channel assumes a duty on the Crown, not on a servant. The placement and maintenance in position of these buoys is work under direction of a general character. As a public accommodation, their maintenance is, in relation to the individual servant, attended to only in the aspect of the duty to the employer. So far as the evidence shows, the direction and responsibility do not go beyond the departmental offices The situation is not, then, one in which a personal liability is engaged by a Crown servant; and there being no basis for the claim against a servant, a prerequisite to a claim under s. 18(*c*) of the *Exchequer Court Act* against the Crown, the action on this ground must fail.

Before leaving this aspect of the case, I might take the liberty of referring to the difficulties in which a claimant against the Crown can be led by the existence in the *National Harbours Board Act* of s. 39, which authorizes

[13] Pp. 814-15

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a limited class of claims in tort against the Crown to be enforced by actions brought against a statutory agent. As already indicated, had the claim been based on some breach by the Crown of duty attaching to ownership or occupation of the harbour, this action was not properly framed to enforce the claim. Instead of being instituted by writ issued out of a District Registry on the Admiralty side, and alleging breach of duty by the statutory agent, the proceeding to enforce such a claim should have been instituted by petition of right filed in the Registry at Ottawa under the *Petition of Right Act,* and should have alleged breach of duty by Her Majesty. Having regard to my findings of fact, I do not think any such claim is fairly arguable. Had the facts been different, I should have been concerned about the fact that there would have been a possible injustice attributable to what might arguably be regarded as procedural irregularities. The proceeding is in the Exchequer Court of Canada, which has jurisdiction, and the defence was conducted by the Deputy Attorney General of Canada who, by the *Department of Justice Act,* R.S.C. 1952, c. 71, would have the conduct of the defence, whichever form the action took. The irregularities are, from a procedural point of view, grave, but I should have been prepared to consider, if the facts had been different, a motion to reconstitute the proceedings in the hope that a means might be found of deciding the case on the merits. Obviously, any such motion, if it were not made until after trial, would have to take into account any possibility that the Crown had been deprived of an opportunity to make a full defence.[14]

The defendant, in addition to its defence on the merits, relies on s. 11(2) of the Statute of Limitations, R.S.C. 1960, c. 370, which reads as follows:

> (2) Where no time is specially limited for bringing any action in the Act or law relating to the particular case, no action shall be brought against any person for any act done in pursuance or execution, or intended execution, of any Act of the Legislature, or of any public duty or authority, or in respect of any alleged neglect or default in the execution of any such Act, duty, or authority, unless

[14] Compare *Hunt v. The Queen* [1967] 1 Ex. C.R. 101, and *North Shipping and Transportation Ltd. v. National Harbours Bd.* (*1967*), per Noël J. (unreported).

> the action be commenced within twelve months next after the act, neglect, or default complained of, or, in case of a continuance of injury or damage, within twelve months next after the ceasing thereof.

This may well be a defence to an action on the Admiralty side of this Court against the person on whose act, neglect or default the claim was based. Compare *Algoma Central and Hudson Bay Ry. Co. v. Manitoba Pool Elevators.*[15] It does not seem to have any application where the claim is one against the Crown in respect of the negligence of a servant even if it is being pursued by way of an action against a defendant nominated by a statutory provision such as s. 39 of the *National Harbours Board Act.*

The action is dismissed with costs.

Toronto 1968
Apr 16-17

BETWEEN:

FREDERICK BURTON, MALCOLM SWARTZ and MARTIN GOLDSMITH, Executors of the Estate of Harry M. Schiller .... APPELLANTS;

AND

THE MINISTER OF NATIONAL REVENUE .... RESPONDENT.

Estate tax—Situs of company shares—Deceased domiciled in Ontario—Shares in Saskatchewan company—No branch register in Ontario—Requirements of Saskatchewan Companies Act—Estate Tax Act, S. of C. 1958, c. 29, s. 9(8)(d).

S, the owner of all the shares in a company incorporated in Saskatchewan, died in 1965 domiciled in Ontario where he kept the register of members. The company's articles of association did not authorize it to keep a branch register, and under the Saskatchewan *Companies Act* it was required to have a registered office in Saskatchewan and to keep there its register of members for entry of particulars of share transfers.

Held, in calculating the deduction authorized by s. 9 of the *Estate Tax Act* the shares could not be deemed to be situate in Ontario under subsec. (8)(*d*)(i) but must be deemed to be situate in Saskatchewan under subsec. (8)(*d*)(ii)(A).

1. Neither the company's registered office (which was a "place of transfer" within the meaning of s. 9(8)(*d*)) nor its register of members (which was a "register of transfers" within the meaning of s. 9(8)(*d*)) were "maintained" for the "transfer of shares" in Ontario as required

[15] [1964] Ex C R. 505.

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by such enactment The company's registered office was in Regina, and in the absence of legal authority to keep the register of members elsewhere, the company's shares could not be effectually dealt with anywhere else. *Erie Beach Co. v. A-G Ont.* [1930] A.C. 161, applied.

2. The shares must be deemed to be situate in Saskatchewan (1) because by virtue of the Saskatchewan *Companies Act* the company maintained there its registered office which was a place of transfer under s 9(8)(*d*) of the *Estate Tax Act,* and alternatively (2) because Saskatchewan was the only province in which the shares could be effectively dealt with. *M.N.R. v. Leckie* [1967] S.C.R. 291, applied.

ESTATE TAX APPEAL.

Gordon W. Ford, Q.C. for appellants.

M. J. Bonner for respondent.

JACKETT P. (orally):—This is an appeal from the assessment under the *Estate Tax Act* of the estate of Harry M. Schiller, who died on May 23, 1965, resident and domiciled in Ontario. The only question involved in the appeal is whether the Minister erred in refusing to allow a deduction under section 9(1) of the *Estate Tax Act* in respect of the shares owned by the deceased at the time of his death in Schiller's Limited, a company incorporated under the *Companies Act* of Saskatchewan.

Section 9(1) of the *Estate Tax Act* provides *inter alia* for a deduction from the tax otherwise payable under that Act upon the aggregate taxable value of the property passing on the death of a person who was domiciled in a prescribed province at the time of his death, of one-half of the part of the tax otherwise payable that is applicable to property passing on the death that was situate in the prescribed province. The parties agree that the deceased in this case was domiciled in Ontario when he died and that Ontario is a prescribed province. The only question in dispute is whether the shares owned by the deceased in Schiller's Limited when he died were situated at that time in Ontario, in accordance with the rules provided by subsection (8) of section 9[1] of the statute for determining such a question for the purpose of section 9.

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[1] (8) A reference in this section to the situs of any property passing on the death of a person shall be construed as a reference to the situs of that property at the time of the death of that person, and, for the purposes of this section except subsection (3), the situs of any property so passing, including any right or interest therein of any kind whatever,

The first rule to be considered as relevant to our problem is, in effect, that "shares...of a corporation...shall be deemed to be situated...in the province where the deceased was domiciled at the time of his death if any register of transfers or place of transfer is maintained by the corporation in that province for the transfer thereof". (Section 9(8)(*d*)(i))

The second rule to be considered, as relevant to our problem, is that, in a case of shares in a corporation to which the first rule does not apply, they shall be deemed to be situated "in the nearest province, relative to the province where the deceased was domiciled at the time of his death, that is not a prescribed province and in which any register of transfers or place of transfer is maintained by the corporation for the transfer thereof". (Section 9(8)(*d*)(ii)(A))

The third rule, to be considered in the event that the problem is not solved by the application of the first two rules, is that that is contained in section 9(8)(*e*) of the *Estate Tax Act.*

As I have already indicated, Ontario is, so the parties agree, a "prescribed province" within the meaning of that

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shall, where that property comes within any of the classes of property mentioned in paragraphs (*a*) to (*e*) of this subsection, be determined in accordance with the following rules:

* * *

(*d*) shares, stocks and debenture stocks of a corporation and rights to subscribe for or purchase shares or stocks of a corporation (including any such property held by a nominee, whether the beneficial ownership is evidenced by scrip certificates or otherwise) shall be deemed to be situated

(i) in the province where the deceased was domiciled at the time of his death, if any register of transfers or place of transfer is maintained by the corporation in that province for the transfer thereof, and

(ii) otherwise,

(A) in the nearest province, relative to the province where the deceased was domiciled at the time of his death, that is not a prescribed province and in which any register of transfers or place of transfer is maintained by the corporation for the transfer thereof,

(B) if no register of transfers or place of transfer is maintained by the corporation for the transfer thereof in any province that is not a prescribed province, in the nearest place outside Canada, relative to the place where the deceased was

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expression in section 9(8)(*d*). Similarly, the parties are in agreement that Saskatchewan, the other province that has to be considered as a possible situs of the shares of Schiller's Limited, is not such a "prescribed province".

The only question that has to be decided as between the parties in this case in connection with the application of the first two rules is whether, at the time of the death of the deceased, Schiller's Limited maintained, in Ontario or in Saskatchewan, "any register of transfers or place of transfer" for the transfer of its shares within the meaning of those words as used in section 9(8)(*d*) of the *Estate Tax Act*.

Schiller's Limited was at the time of the death of the deceased governed by the *Companies Act*, R.S.S. 1953, chapter 124, as amended by chapter 18 of the Statutes of 1956. Schiller's Limited was incorporated as a memorandum of association company (R.S.S. 1953, chapter 124, sections 5, 19 and 20). A company incorporated under the Saskatchewan Act must have a registered office in Saskatchewan (section 97), and must keep in that registered

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ordinarily resident at the time of his death, in which any such register of transfers or place of transfer is so maintained,

(C) if no register of transfers or place of transfer is maintained by the corporation for the transfer thereof in any province that is not a prescribed province or in any place outside Canada, then in the nearest province, relative to the province where the deceased was domiciled at the time of his death, that is a prescribed province but is not a designated province and in which any such register of transfers or place of transfer is so maintained, or

(D) if no register of transfers or place of transfer is maintained by the corporation for the transfer thereof in any province that is not a prescribed province, in any place outside Canada, or in any province that is a prescribed province but is not a designated province, then in the nearest province, relative to the province where the deceased was domiciled at the time of his death, that is a designated province and in which any such register of transfers or place of transfer is so maintained;

(*e*) property for which no specific provision is made in any other paragraph of this subsection, or the situs of which, determined as provided therein, cannot with reasonable certainty be identified, shall be deemed to be situated in the place where the deceased was domiciled at the time of his death;

and, for the purposes of subsection (3), the situs of any property so passing, including any right or interest therein of any kind whatever, shall, where that property comes within any of the classes of property mentioned in section 38, be determined as provided in that section.

office (section 76 as enacted by chapter 18 of 1956 read with section 78a as enacted by section 6 of chapter 18, and section 76 as it existed prior to 1956) a "register of its members" in which it must enter *inter alia* "particulars of the transfer of any member of his shares" (section 76). That register is evidence of the matters directed or authorized to be inserted therein (section 76). Either the transferee or transferor can require the company to enter in its register of members the name of a transferee (section 77) and may enforce its demand by applying to the Court of Queen's Bench of Saskatchewan for rectification (section 78). Such a company may have a branch register of members outside Saskatchewan if so authorized by the regulations in its Articles of Association (section 83). A share in such a company is personal estate, transferable in manner provided by the articles of the company (section 11). A reference to the articles in this case shows that a transfer is effected by registering it on the register of members.

The registered office of Schiller's Limited has been in Regina, Saskatchewan since it was incorporated in 1927. From the time of its incorporation, it had a "Shareholders' Register" which, I am satisfied, is the register of members required by the statute. It has never had authority in its regulations for a branch register. The Shareholders' Register was kept at the registered office at Regina until May 1953, when the deceased (who until his death in 1965 owned all the company's shares, was president of the company, and exercised "full...control and management..." of the company) changed his own place of residence and domicile from Regina to Toronto and took the Shareholders' Register with him. After the move, the deceased dealt with the Shareholders' Register in Toronto as though it were in Regina where the law required that it be.

In so far as Schiller's Limited is concerned, I am of the view that its Shareholders' Register, which, as I have already indicated, is in my view the "register of members" that it was required by the *Companies Act* to keep, was a "register of transfers" within section 9(8)(*d*) of the *Estate Tax Act,* that its "registered office" was a "place of transfer" within that section, and that both the Shareholders' Register and the registered office were "maintained" by the

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company *inter alia* "for the transfer" of shares in the company as required by the Saskatchewan law under which the company operates. I come to that conclusion by reason of the view that the "transfer" contemplated by section 9(8)(*d*) is one that is effective as between the holder of the shares and the company, and not one that is merely effective between transferor and transferee.[2]

Having reached that conclusion, I have to decide whether either the Shareholders' Register or the registered office was maintained by the company in the Province of Ontario for the transfer of its shares. Clearly, the registered office was not maintained in Ontario. With reference to the Shareholders' Register, there was no legal authority to keep it anywhere other than at the registered office in Regina. It seems clear from the decision in *Erie Beach Co. Ltd. v. Attorney-General for Ontario*[3] that, whatever the deceased thought he was accomplishing by what he did with the register in Toronto, it did not operate, because it could not in law operate, to "effectually deal" with the company's shares. That being so, it cannot be said that the register was being "maintained" in Ontario as a register of transfers. I conclude, therefore, that the company was not maintaining a "register of transfers" in Ontario for the transfer of its shares. It follows that the appellant fails in its contention that the shares are deemed, by virtue of section 9(8)(*d*)(i), to have been situated in Ontario when the deceased died.

Turning to section 9(8)(*d*)(ii)(A), I have concluded that the company was, at the relevant time, maintaining its "registered office" in Regina and that it was a statutory function of that office to serve as a "place of transfer" for the transfer of the company's shares. The registered office is the place where a transferee or transferor was entitled to go under sections 77 and 97 and demand that a transfer be registered, and, if the company failed to comply, application could be made to the Court under section 78 to compel it to do so. The fact that the physical register of transfers

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[2] See *Rex v. Williams,* [1942] A.C. 541 and *Royal Trust Company v. The King,* [1949] S.C.R. 329, as applied by Mr. Davis in *Leckie Estate v. Minister of National Revenue,* 65 DTC 744, whose judgment was approved by the Supreme Court of Canada in the same case [1967] S.C.R. 291 at page 294.

[3] [1930] A.C. 161.

had wrongfully been removed from the registered office did not make that office any the less a "place of transfer". The company in fact maintained a registered office in Saskatchewan. As a matter of law, that office had the character of being a "place of transfer". It follows that my conclusion is that the shares in question were, by virtue of section 9(8)(*d*)(ii)(A), deemed to have been situated at the material time in Saskatchewan. I do not, therefore, have to consider the respondent's alternative argument that the Shareholders' Register was maintained by the company in Saskatchewan notwithstanding its physical situs in Toronto for over twelve years, or the question as to whether section 9(8)(*e*) of the *Estate Tax Act* can have any application to shares in a company notwithstanding that section 9(8)(*d*) seems to have been intended as a comprehensive set of rules re situs for shares.[4]

There is another somewhat simpler line of reasoning which leads me to the same conclusion as that that I have reached by considering the matter step by step. In *Leckie Estate v. Minister of National Revenue*[5], the Tax Appeal Board had to consider a problem under section 9(8)(*d*) at a time when it was somewhat differently worded but when it was, as far as my use of the decision is concerned, in substance the same as the present section 9(8)(*d*). The facts that the Board had to consider were similar to those in the present appeal except that the controlling shareholder did not take the register of transfers away from the home province of the company. In that case Mr. Davis, who gave the decision of the Board, after examining the *Erie Beach* case *supra,* and other cases of that line of cases, concluded that Winnipeg, Manitoba was the only place where shares of the corporation in that case could be effectively dealt with and concluded from that that "the situs of the shares... must be found to have been in the Province of Manitoba... within the meaning of section 9 of the *Estate Tax Act*". Mr. Davis's reasons on this point were expressly adopted by the Supreme Court of Canada. See *Minister of National Revenue v. Leckie*[6] per Cartwright J., as he then was, delivering the judgment of the Court, at

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[4] This intention appears clearer when section 9(8)(*d*)(ii) is considered as it was prior to the 1962-3 amendment.

[5] 65 DTC 744.

[6] [1967] S.C.R. 291.

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page 294. It seems obvious to me that the basis of Mr. Davis's reasoning is that a company cannot be regarded as maintaining a register of transfers or a place of transfer any place where the shares cannot be effectively dealt with and must be regarded as maintaining such a register or place any place where the shares can be effectually dealt with.

Applying that reasoning to this case, reading the Saskatchewan *Companies Act* in the light of the *Erie Beach* case, it is clear that the only place where Schiller's Limited's shares could, at the relevant time, have been effectively dealt with, is some place in Saskatchewan. It therefore follows that the situs of its shares must be found to have been in that province within the meaning of section 9 of the *Excise Tax Act*.

The appeal is dismissed with costs.

Toronto
1968
Apr. 9-11, 17

BETWEEN:

SETTLER OILS LIMITED ....APPELLANT;

AND

THE MINISTER OF NATIONAL REVENUE .... RESPONDENT.

Income tax—Company formed to acquire mineral rights of dormant company—Oil leases for lump sum payments and royalties on production—Whether lump sums taxable—Whether revenue from a business—Relevance of incorporator's object to liquidate property—Whether price of properties deductible in computing income from leases.

Appellant company, its primary object being to deal in mineral properties, was incorporated in 1952 at the instance of *C* and her children who held all the shares therein. Appellant purchased at an appraised value of $17,500 certain mineral rights in western Canadian lands which were the sole remaining assets of *S* Co., which had been originally incorporated in 1882 to deal in land, and 85% of whose capital stock was held by *C*. This course was decided on by *C* because of the uncertain value of the mineral rights, the problem of succession duties on her death, and because the minority shareholders in *S* Co. were dead or untraceable. Between 1954 and 1963 appellant company granted a number of oil leases to oil companies from which it received lump sum "bonus payments" as well as production royalties. Appellant was assessed to income tax in respect of bonus payments of $16,000 received in 1961, $32,000 in 1962 and

$183,984 in 1963, and appealed contending that such payments were not taxable because the company's sole purpose in acquiring the mineral rights was to dispose of or liquidate them.

Held, notwithstanding that such may have been appellant's intention the lump sum payments were revenue from a business and therefore taxable. *Hudson's Bay Co. v. Stevens* 5 T.C. 424; *C. H. Rand v. Alberni Land Co.* (1920) 7 T.C. 629; *Com'r of Taxes v. British Australian Wool Realization Assoc. Ltd.* [1931] A.C. 224; *Glasgow Heritable Trust Ltd. v. C.I.R.* (1954) 35 T.C. 196, distinguished. *Balstone Farms Ltd. v. M.N.R.* [1968] S C.R. 205; [1968] C.T.C. 38; *Western Leaseholds Ltd. v. M.N.R.* [1960] S.C.R. 10, applied.

Held also, no part of the $17,500 paid for the mineral rights was deductible from the lump sums received in 1962, 1963 and 1964 under the leasing contracts. This was not a case of a sale of stock-in-trade. *Berkheiser v. Berkheiser et al* [1967] S C.R. 387, applied.

INCOME TAX APPEAL.

D. J. Wright, Q.C. and *Warren S. Seyffert* for appellant.

D. G. H. Bowman and *F. P. Dioguardi* for respondent.

JACKETT P. (orally):—This is an appeal from the appellant's assessments under Part I of the *Income Tax Act* for the taxation years 1961, 1962 and 1963. The sole ground of appeal is that the assessments are excessive by reason of the inclusion in the computation of the appellant's incomes for the years in question of certain amounts that, according to the appellant, should not have been so included. The amounts that the appellant says were wrongly included in computing its incomes are $16,000 for 1961, $32,000 for 1962, and $183,984 for 1963.

The facts upon which the assessments were based are not really in issue and can be summarized briefly. The appellant was incorporated on June 13, 1952, and the primary object set out in its charter reads as follows:

> (a) to purchase or otherwise acquire, sell, lease, dispose of and otherwise deal with oil, coal and natural gas claims, lands and mineral rights and properties supposed to contain oil, coal and natural gas and undertakings connected therewith;

On September 16, 1952, the appellant acquired, by purchase from a company known as Saskatchewan Land and Homestead Company Limited (hereinafter referred to as "Saskatchewan"), for a consideration of $17,500, the fee simple title to the mineral rights in a substantial acreage of land in Western Canada. During the period from 1954 to 1963, the appellant entered into a number of agreements

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(commonly referred to as oil leases or options to lease) with oil companies who wished to explore for oil in the areas in question. Under each of such agreements, the appellant conferred on the oil company the right, during a special period, to search for oil, and the right to remove any oil found, on terms that certain lump sums (called "bonus payments") would be paid by the oil company to the appellant upon the execution of the agreements (and that certain annual payments, called "delay rentals", would be made during any part of the specified period before the oil company commenced to drill for oil) and that the oil company would be entitled to retain out of any oil so removed 87½ per cent for itself, and would hold 12½ per cent for the appellant. It is common ground that, at the time that the appellant acquired the mineral rights from Saskatchewan, it was the intention that it would enter into transactions of that character, if and when it became possible for it to do so. The amounts in dispute are lump sum amounts received in the years in question under such contracts.

If there were no facts other than the ones that I have just summarized, there would not appear to be any real doubt that the amounts in question were properly included in computing the appellant's incomes for 1961, 1962 and 1963, respectively, as being revenues from a "business" within the extended meaning of that word as defined by section 139(1)(*e*) of the *Income Tax Act*. Compare *Minerals Ltd. v. M.N.R.*,[1] *Western Minerals Ltd. v. M.N.R.*,[2] and *Western Leaseholds Ltd. v. M.N.R.*[3] Having regard to the conclusion that I have reached, I will not deal with the alternative arguments that, even if there was no "business", these payments would have an income character as being profits from property,[4] or by virtue of section 6(1)(*j*) of the *Income Tax Act*.

[1] [1958] S.C.R. 490. [2] [1960] S.C.R. 24.

[3] [1960] S.C.R. 10.

[4] I am unable to distinguish the leases involved here from the "lease" that was the subject matter of the decision in *Berkheiser v. Berkheiser et al.,* [1957] S.C.R. 387. As I understand that decision, while such a lease is, from one point of view, a sale of property—that is, a sale of the minerals when removed—it is not a conveyance of the minerals *in situ,* title to which remains in the lessor, and both the rents and royalties are "profits" and "like rent from a leasehold" are embraced

The facts upon which the appellant relies for its contention that the amounts in question were not, properly considered, revenues from a business within the meaning of that word as used in the *Income Tax Act* were developed in some detail commencing with the time when Saskatchewan was incorporated in 1882. Those facts, in so far as I appreciate their significance for the purpose of the appellant's contention, may be summarized as follows:

(a) Saskatchewan, during its early years, acquired land in Western Canada for resale under agreements of sale to settlers. (In fact, apparently, much of the land was resold, either by Saskatchewan or the mortgage company, under agreements that reserved the mineral rights to Saskatchewan.)

(b) In the early part of this century, there were internal troubles in the administration of Saskatchewan that resulted in protracted litigation, and such litigation effectively brought an end to Saskatchewan's land disposition business.

(c) By the time the litigation came to an end, the "moving force" in the company was a lawyer by the name of A. B. Cunningham who had been acting for the company in this litigation and who had put a great deal of effort and money into carrying on the litigation. He had also become a substantial shareholder in Saskatchewan.

(d) The litigation also left Saskatchewan with debts substantially in excess of what could be readily realized from its assets.

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in a devise of the title to the land. See the judgment of Rand J. and Cartwright J. (as he then was) at pages 394-5. Even though there is no conveyance of legal title to the land, but only a sale of something to be taken from the land, the appellant's operations may nevertheless constitute the carrying on of a "business" within the meaning of the words as used in the *Income Tax Act*. Compare *Orlando v. Minister of National Revenue,* [1962] S.C.R. 261. While I am unable, as I see the matter, without more mature consideration, to escape the conclusion that the payments in dispute are, in any event, income of the appellant from property, in which event the appellant's contention based on the "liquidation" and "disposition" cases would have no application, I have chosen to deal with the matter on the basis of the respondent's principal contention, which was that the appellant's operations constitute the carrying on of a business.

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(e) During the 1920's and 1930's, as a result of a depression in the western provinces, Saskatchewan went into default under a mortgage on its lands and in respect of its liability to a bank.

(f) The mortgage company thereupon took over the management of the winding-up of Saskatchewan's affairs; and the shares of Cunningham and others in Saskatchewan were assigned to the mortgage company and the bank.

(g) A. B. Cunningham died in 1932 leaving a widow and eight children. His estate was left to his widow, who was executrix of his will, but the estate did not appear to be sufficient to warrant the expense of probate.

(h) In 1944, the mortgage company, having realized almost enough to pay off its claim, the bank and Saskatchewan agreed that the bank would take over Saskatchewan's remaining lands in full satisfaction of its claim. The shares in Saskatchewan were then returned to the estate of A. B. Cunningham. As a result, Saskatchewan was left with nothing except the mineral rights that had been reserved to it, which were understood at the time to be of no value.

(i) Saskatchewan remained, after the 1944 arrangement, for all practical purposes, dormant, until 1948, when it became aware, as a result of an offer made to it by an oil company, that its mineral rights had some value. Its corporate affairs were then put in order and Mrs. Cunningham and two of her sons were elected as its officers, and took over its active administration.

(j) In June 1948, Saskatchewan granted an option to lease all of its mineral rights of which its management was then aware to an oil company, and received, under the option contract, in 1948 and 1949, payments totalling $43,085.95. Eventually, the oil company took a lease under that option.

(k) While the Department of National Revenue originally took the position that the 1948-49 payments were income, eventually it conceded that they were not taxable under the *Income Tax Act*.

(l) In or about 1951, Saskatchewan discovered that it owned mineral rights of which it had not previously been aware, and that it therefore still had assets of value to be disposed of although there was not then much activity in the area where those mineral rights were.

(m) At that time (i.e. after the discovery of the existence of additional mineral rights), as the Cunningham family saw it, there was a potential succession duty problem by reason of the fact that Mrs. Cunningham was almost eighty years of age and owned about 85 per cent of Saskatchewan's shares, and the fact that it was impossible to make an accurate determination of the value of the mineral rights. Her family, moreover, were anxious that she should receive some of the proceeds from realization during her lifetime. The situation from their point of view was "further complicated by the fact that the remaining 15 per cent of Saskatchewan's outstanding shares were registered in the names of shareholders, most of whom were deceased or untraceable". For those reasons, it was decided by Mrs. Cunningham and her children to incorporate a new company, all the shares of which would be owned by the Cunningham family to acquire Saskatchewan's mineral rights, which were Saskatchewan's only assets other than cash and bonds at the time, "for a cash consideration based upon appraisal". They also decided that Saskatchewan should then be wound up and that the interests of the unknown or untraceable shareholders should be paid to the Public Trustee. Before proceeding with this plan, a ruling was obtained from the Department of National Revenue that the shareholders in Saskatchewan would not be taxable on the distribution on its winding up.

(n) The appellant was incorporated by the Cunningham family on June 13, 1952, pursuant to this plan and, as already indicated, purchased Saskatchewan's mineral rights (including the mineral rights which had already been leased to an oil company by Saskatchewan) for $17,500. Saskatchewan thereupon distributed its assets to its shareholders and surrendered its charter. Mrs. Cunningham subscribed for preferred shares in the appellant in the amount of $17,500, which amount was

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used by the appellant to pay for the mineral rights purchased from Saskatchewan. Ordinary shares were issued at $1 per share as follows:

(a) Mrs. Cunningham	16 shares
(b) Each of the eight children, 8 shares or	64 "
TOTAL:	80 "

Certain other facts were also established. In 1954, the appellant agreed to lease to the oil company with whom Saskatchewan did business in 1948 and 1949 the mineral rights that came to its attention in 1951 and received as a result amounts of $36,274.60 and $15,361.09, which the Department of National Revenue decided not to include in its income for the purpose of the *Income Tax Act*. Eventually, that oil company abandoned all its rights in respect of its leases from the appellant except in respect of lands where oil had been discovered "and the full mineral rights in respect thereof automatically reverted again to the appellant". The discovery of a new field in 1956 resulted in the appellant being able to grant further options and leases in respect of the "reverted mineral rights" which resulted in the lump sum payments now in question. All told, in addition to the lump sum payments to which I have referred, the appellant has received royalty payments (i.e. under its right to 12½ per cent of production) amounting to about $1,500,000, and it has received a depletion allowance under the *Income Tax Act* of 25 per cent in respect of such payments.

Throughout the evidence put forward on behalf of the appellant, it has been contended that the intention of those who have constituted the management of Saskatchewan and the appellant since the discovery of value in the mineral rights in 1948 has been to dispose of or liquidate the assets of the respective companies. In this connection, it has been testified that the only practical way of *disposing* of oil rights in Western Canada during the period in question was to grant leases or options of the kind that I have already described. I accept it that the only sensible way whereby the legal owner of mineral rights having a value by reason of the possible presence of oil could have turned them to advantage, if he were not in a position to explore and develop himself, was to enter into such arrangements. This would appear to have been the only businesslike course of action for any person owning such rights and desiring to turn them to advantage. I have difficulty, however, in regarding such contracts as being dispositions of the mineral rights themselves although I recognize that, in the case of a wasting asset such as oil, once the lessee has exercised his rights by removing all the oil, the mineral rights will have little more than a theoretical value unless and until some other mineral is discovered.

The contention that the intention of the appellant was exclusively that of disposing or liquidating the mineral rights was put forward on the apparent assumption that there is a doctrine or principle established by the so-called "disposition" or "liquidation" cases that, where a company's sole purpose in acquiring property is to dispose of it or to liquidate it, it is not taxable under the *Income Tax Act* on any profit that it may make in the course of such disposition or liquidation. The cases relied upon by the appellant in this connection are *Hudson's Bay Co. v. Stevens*[5], *C. H. Rand v. Alberni Land Co.*[6], *Com'r of Taxes v. British Australian Wool Realization Assoc. Ltd.*[7], *Glasgow Heritable Trust Ltd. v. C.I.R.*[8]

In my view, none of these cases have any application to the facts of this case which, as I understand them from this point of view, do not differ in principle from the facts under consideration in *Balstone Farms Ltd. v. M.N.R.*[9]

The only principle involved in the problem that I have to decide, as I understand it, is that, by virtue of the *Income Tax Act,* a taxpayer is taxable on any profit for a year from a business. The so-called disposition or liquidation cases do not establish any different principle. They are merely cases where it was found as a fact that the taxpayer was not carrying on a business. The problem I have to solve is therefore merely a question as to whether the amounts in question are revenues from a business.

As I have said, what was decided in each of the cases on which the appellant relies is that the company three

[5] 5 T.C. 424. [6] (1920) 7 T.C. 629.
[7] [1931] A.C. 224. [8] (1954) 35 T.C. 196.
[9] [1968] S.C.R. 205; [1968] C.T.C. 38.

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involved did not receive the amounts in dispute as profits from a business. In the *Hudson's Bay Co.* case, a great exploration company was held not to be carrying on a business when it was disposing of the lands it had received in place of those received by it by way of a grant from the Crown as an incentive to its exploration of unknown lands. In the *Rand* case, a company was employed as "machinery" by private landowners to properly realize the capital of their property "under the peculiar circumstances of their divided title". In the *British Australian Wool* case, the company received the property in question under a scheme pursuant to which it was to dispose of the property and distribute the proceeds to specified parties. In the *Glasgow Heritable Trust* case, real property acquired by a partnership for resale in the course of a business became unmarketable by reason of new legislation so that the business came to an end and there was no alternative but to hold the property and salvage as much as possible by disposing of it as and when that became possible.[10] The company in question was incorporated in that case as machinery for this long-run salvage operation. As pointed out by Judson J. in *Balstone Farms Ltd. v. M.N.R.*[11]: "In none of these realization cases was there an out and out transfer by former owners for a cash consideration." On the one hand, in the *Hudson's Bay Co.* case, there was a mere realization by the owner of property and there was not "a sale in execution of a profit-making enterprise, either 'adventure', or 'trade', or 'business' ".[12] On the other hand, in the other cases, the property was put into the hands of the company in question for the benefit of the former owners or persons nominated by them.

The appellant's acquisition is not at all similar to any of such cases. The appellant bought the property in question for a price based on an appraised value which, for present purposes, I must assume was a fair price because one purpose of the transaction was to bring to an end the very real interest that the 15 per cent minority shareholders in Saskatchewan had in the possible increase in the value

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[10] Compare *Minerals Ltd. v. M.N.R.*, [1958] S.C.R. 490, per Martland J. at p. 497.

[11] [1968] S.C.R. at p. 212; [1968] C.T.C. at p. 41.

[12] See *Anderson Logging Co. v. The King*, [1925] S.C.R. 45, per Duff J., at p. 58.

of what Saskatchewan sold to the appellant. It is quite clear that the appellant was not to dispose of, or liquidate, the property for the benefit of Saskatchewan, which was to be wound up, or for the benefit of Saskatchewan's shareholders, 15 per cent of whom were to have no interest in the proceeds of the disposition of the property by the appellant, but were to accept their share of the $17,500 in lieu of what their interest in the disposition of the property might have been if Saskatchewan had retained it.

Indeed, the appellant acquired the property in question, as every trader acquires his stock in trade, in the hope that it might realize from it more than it paid for it, but knowing that the proceeds of realization might possibly be less than that amount. Any amount it might realize in excess of what it paid was to go, in the ordinary course of corporate operations—by way of dividends or on winding up—to its shareholders—that is, the members of the Cunningham family—and would not benefit any other person, and in particular would not benefit any of the 15 per cent minority shareholders in Saskatchewan. I cannot distinguish the acquisition of the property in question by the appellant and its subsequent turning of that property to its advantage from what happened in *Minerals Ltd. v. M.N.R.*, *Western Minerals Ltd. v. M.N.R.*, and *Western Leaseholds Ltd. v. M.N.R.*, to which cases I have already referred. I refer to the judgment of the Supreme Court of Canada in *Western Leaseholds Ltd. v. M.N.R.*, per Locke J. at pages 21-2, where he used language that applies equally to this case when he said:

> In *Anderson Logging Company v. The King*, Duff J., as he then was, said that if the transaction in question belongs to a class of profit-making operations contemplated by the Memorandum of Association, *prima facie* at all events the profit derived from it is a profit derived from the business of the company. That presumption may, of course, be negatived by the evidence as was done in the case of *Sutton Lumber & Trading Company v. The Minister of National Revenue*. In the present case, however, the evidence, far from negativing the presumption, appears to me to support it.

I have come to a conclusion against the appellant on the main branch of the appeal.

In the alternative, the appellant contended that, if the amounts in dispute were properly included in the computation of its income for the years in question, it was entitled to a deduction in the same years of some part of the price

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of $17,500 that it paid for the mineral rights. No suggestion was made as to what part of that price should be allowed as a deduction for any particular year or as to what principle should be applied in determining the amount of each deduction. This is not a case of buying stock-in-trade and selling it. The principles applicable to such a case are well settled. See *Minister of National Revenue v. Irwin.*[13] In this case, the appellant at no time sold what it purchased. If it had, it would have been entitled to deduct the cost to it of what it sold even though it were difficult to work out the actual allowance. Compare *British South Africa Co. v. Com'r of Income Tax.*[14] However, this is not such a case. What the appellant did in this case was grant certain "leases" of its mineral rights that did not differ in character from the mineral lease under consideration in *Berkheiser v. Berkheiser.*[15] It never parted with title to its mineral rights. Nothing is deductible in such a case. Compare *Alianza Co. v. Bell.*[16] Just as nothing is deductible from ordinary rentals of real property in respect of the cost of the simple title to the property that has been leased, so nothing is deductible here from the payments (that are of the same character as ordinary rental payments according to the *Berkheiser* decision) in respect of the cost of the fee simple title to the mineral rights. It is because there is no deduction for cost in such a case that a depletion allowance is granted in respect of the oil actually removed from the land. In this case, the appellant has been allowed such a depletion allowance equal to 25 per cent of over a million and one-half dollars in royalties, being the 12½ per cent of production received by it.

The appeal is dismissed with costs.

[13] [1964] S.C.R. 662.

[14] [1946] A.C. 62.

[15] [1957] S.C.R. 387.

[16] [1906] A.C. 18.

Toronto 1968

Apr. 2-4

Ottawa

Apr. 17

ONTARIO ADMIRALTY DISTRICT

BETWEEN:

CLUB COFFEE COMPANY LIMITED ....PLAINTIFF;

AND

MOORE-McCORMACK LINES, INC., MOORE-McCORMACK LINES (CANADA) LIMITED and EASTERN CANADA STEVEDORING (1963) LTD. .... DEFENDANTS.

Shipping—Damages—Shipment of coffee—Bill of lading giving U.S. port as destination—Substitution of bill of lading with Montreal as destination while ship at sea—Portion of cargo not delivered—Customs duty paid by consignee—Whether recoverable as damages—U.S. Carriage of Goods by Sea Act—Inapplicability of—Clause in bill of lading re valuation of goods lost—Effect of on computation of damages.

The *Mormacisle* carried 500 bags of coffee from Rio de Janeiro to Montreal, the coffee being originally covered by a bill of lading giving its destination as New York or Boston at owner's option, but before the ship reached a United States port that bill of lading was surrendered to the shipowner at New York who issued in its place two bills of lading, each for 250 bags of coffee, with Montreal as destination The *Mormacisle* touched at New York and Boston before arriving with the coffee at Montreal where plaintiff, who held one of the bills of lading, paid customs duty on 250 bags of coffee. Plaintiff did not receive delivery of 92 bags and 80 pounds of coffee and sued the shipowner and the ship's agent for damages A clause in plaintiff's bill of lading declared that in calculating claims the value of the goods should be invoice price plus freight and insurance if paid and that it should be construed according to the law of the United States Under the Canadian *Customs Act* duty was payable on the coffee when the *Mormacisle* entered Canada and defendants knew that no refund of duty for the undelivered coffee would be made unless the shipowner produced a satisfactory explanation, which it did not do.

Held, the customs duty paid on the lost coffee was an element of plaintiff's damages resulting from the non-delivery of the coffee

1. The damages recoverable for a shipowner's failure to deliver goods are not restricted to the value of the goods but include customs duty which the owner of the goods has paid or become liable to pay thereon. *Town of Weston v The Steamer Riverton* [1924] Ex. C.R 65, *S S Ardennes (Cargo Owners) v. S.S. Ardennes (Owners)* [1951] 1 K B 55, distinguished.

2. While s 3(8) of the United States *Carriage of Goods by Sea Act* would if it applied render void the clause in the bill of lading as to valuation of goods, that statute applies only to contracts of carriage to or from United States ports and so did not apply here following the substitution of bills of lading; but in any event that clause in the bill of lading merely provides for the calculation of the value of

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goods as an element in the calculation of damages for non-delivery, and the right to recover the customs duty paid thereon as another element of such damages is not affected thereby.

ACTION for damages.

D. L. D. Beard for plaintiff.

E. M. Lane and *Norman M. Chorney* for defendants.

THURLOW J.:—In this action the plaintiff claims damages resulting from the failure of the defendants to deliver part of a shipment of coffee carried in the first named defendant's ship *Mormacisle* on a voyage from Rio de Janeiro to Montreal. Neither the loss of the coffee nor the right of the plaintiff to recover its value is in dispute, nondelivery of 92 bags and 80 pounds of the coffee included in the shipment being admitted, but issue arises on the claim of the plaintiff that the damages recoverable in respect of the loss include Canadian Customs duty which it paid on the lost coffee. The plaintiff's claim also included items in respect of customs brokerage and expenses of a letter of credit but these were abandoned in the course of the argument.

The defendant Moore-McCormack Lines Inc. is a United States corporation and the defendant Moore-McCormack Lines (Canada) Limited is its Canadian subsidiary and agent in Canada. No issue has been raised as to which of these two defendants, who are herein referred to as the "defendants", is liable to the plaintiff for the loss. The plaintiff's claim as against the third named defendant was abandoned in the reply and the action as against that defendant has been discontinued.

When the *Mormacisle* left Rio de Janeiro the shipment of coffee, consisting of some 500 bags of coffee, was destined for New York or Boston, at the option of its owner, under a contract evidenced by a bill of lading issued by the first named defendant on November 4, 1964. On November 18, 1964, however, when the ship was at sea and had not yet reached any United States port this bill of lading was surrendered by its holder to the first named defendant in New York with a request by letter that the ladings be split in the manner therein mentioned and that the port of discharge be Montreal. The first named defendant thereupon issued at New York two bills of lading each for 250 bags of coffee showing Rio de Janeiro as the port of loading and Montreal as the port of discharge. The plaintiff is the holder of one of these two bills of lading.

After the issuance of these bills of lading the *Mormacisle* touched at several United States ports including New York and, finally, Boston whence she proceeded directly to Montreal and arrived there on December 7, 1964. The whole of the coffee was thereupon reported by the second named defendant or the master of the ship, or both, to the Canadian customs authorities as being on board and on December 15 the plaintiff, who had previously instructed Smith Transport to bring the coffee from Montreal to Toronto in bond, through its brokers made a customs entry at Toronto for the whole of the coffee showing 132 bags as received and 118 bags to follow and in accordance with what was admitted on discovery to be the practice, paid the duty at 2 cents per pound on the whole 250 bags of coffee. Thereafter on December 29, 1964, 26 bags were received but 92 bags and 80 pounds of the coffee were never delivered.

At some point, either shortly before or shortly after the arrival of the *Mormacisle* in Montreal (the precise date does not appear), the defendants sent to the plaintiff at Toronto an arrival notice which consisted of an invoice for the ocean freight on the 250 bags of coffee referring to them as "in bond", mentioning the name of the ship and the number of the bill of lading and including a notice in the following terms:

> The above mentioned vessel is now in port with goods as described for your account. You are requested to pass Customs entry and take delivery without delay. It is in your interest to do so promptly and thereby avoid Harbour penalty charges assessed.

A further invoice for the ocean freight on the 250 bags of coffee was dated January 14, 1965 and was paid by the plaintiff on January 18, 1965. The shortage of 92 bags had, however, been reported to the defendants on December 28, 1964, in a preliminary report by the third named defendant, a stevedoring company, which had been employed by the defendants to discharge the ship's cargo. The report in question indicated that the 92 bags could not be located after the discharge of the cargo.

By sections 19 to 22 of the *Customs Act* every importer of goods by sea from any place out of Canada is required

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within three days after the arrival of the importing vessel to make a customs entry of such goods containing a description of them and of their quantity and value and other details, to deliver, as well, an invoice showing the place and date of their purchase and other details, and, unless the goods are to be warehoused in the manner provided by the Act, to pay down at the time of entry all duties upon all such goods entered inwards. By section 100, for the purpose of levying any duty the importation of any goods, if made by sea, is deemed to have been completed from the time such goods were brought within the limits of Canada and by section 101, the true amount of customs duty payable with respect to any goods imported into Canada, from and after the time when such duties should have been paid or accounted for, constitute a debt due and payable to Her Majesty, jointly and severally from the owner of the goods at the time of their importation and from the importer thereof. By section 111(1), it is provided that no refund of duty is to be allowed because of any alleged inferiority or deficiency of quantity of goods imported and entered and which have passed into the custody of the importer under permit of the collector, or because of the omission in the invoice of any trade discount, or other matter or thing, that might have the effect of reducing the quantity or value of such goods for duty, unless the same has been reported to the collector within 30 days of the date of entry or delivery or landing, and the said goods have been examined by the said collector or by an appraiser or other proper officer and the proper rate or amount or reduction certified by him after such examination. Section 111(2) goes on to provide that all applications for refund of duty in such cases shall be submitted with the evidence and all particulars for the decision of the Minister, who may order payment on finding the evidence sufficient and satisfactory.

It may be added that the defendants were at all material times aware that customs duty at 2 cents per pound was payable on the importation of coffee into Canada and were also aware that no claim by an importer for a refund of duty paid on cargo would be allowed in a case of this kind save on production by the shipowner within 30 days of an amending declaration stating that the lost goods which had been shown on the ship's report inwards as being on board, were not in fact imported into Canada and a short landing certificate supported by documents establishing either that the goods had never been loaded on the ship or that they had been discharged before the ship reached a Canadian port or had been lost at sea.

The effect of the provisions of the *Customs Act* to which I have referred appears to me to be that if the 92 bags of coffee were brought into Canada the plaintiff became liable for customs duty in respect of them whether it ultimately received them or not. However, even though they were reported by the Master of the ship and entered by the plaintiff as having been imported the plaintiff would not have been liable for duty in respect of them if they were not actually imported into Canada and by following the procedure prescribed by section 111 would have been entitled to a refund of the duty paid on them on satisfying the Minister that the missing goods had not in fact been imported into Canada. Short of satisfying the Minister on that point, however, it does not appear to me that any refund would have been obtainable. At the same time it is also apparent that the plaintiff, whose goods were not delivered, could have no means of satisfying the Minister of the material fact unless the defendants could provide evidence of it. This, however, they did not do and I think the inference is plain that they did not do so because they were not able to substantiate the fact. With this must I think be considered the fact that Mr. Jewell, in the course of his examination for discovery given on behalf of both defendants stated that the ship went directly from Boston to Montreal, and that "to our knowledge" the coffee was still on board when the ship left Boston.

In most cases of this kind the measure of the damages recoverable for failure to deliver goods is the value of the goods at their destination at the time they should have been delivered pursuant to the contract of carriage and it is, I think, for this reason that in many expressions of judicial opinion the measure of such damages has been referred to as being the value of the goods. The true measure of such damages, however, was, I think, somewhat more accurately

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expressed by Lord Esher, M.R. in *Rodocanachi v. Milburn*[1] when he said, at page 76:

> I think that the rule as to measure of damages in a case of this kind must be this: the measure is the difference between the position of a plaintiff if the goods had been safely delivered and his position if the goods are lost.

So expressed the measure of damages appears to me to coincide with the principle of *restitutio in integrum* and to be broad enough to include the whole of the owner's loss including, where the goods have reached Canada and he has thus become liable for customs duty on them, the amount of such duty. This, to my mind, becomes an element in the assessment of the damages flowing from the failure of the shipowner to deliver the goods at the port of discharge in the same way as the freight becomes an element to be taken into account. If the freight has not been paid it is deducted from the market value of the goods at the port of discharge in measuring the damages for failure to deliver because the owner would have had to pay it if the goods had been delivered. But if it has been paid it does not enter into the computation since the owner having paid the freight is entitled to the value of his goods landed at the port of discharge. In the same way, it appears to me that the owner of the goods having paid the freight and either paid or become liable for the customs duty is entitled to enough to replace them by purchase of like duty paid goods at the port of discharge. It is I think of some importance as well to remember that what the owner is entitled to recover in respect of the shipowner's failure to deliver his goods is damages, and that the value of the lost goods is but an element to be taken into account in assessing such damages. In my opinion such damages also include customs duty which the owner has paid or become liable to pay on the undelivered goods.

It was submitted on behalf of the defendants that the plaintiff was not obliged to enter and pay the duty on the whole of the shipment until it was delivered to him in bond but it does not seem to me to lie well with the defendant, who had advised the plaintiff of the arrival of its goods in Canada and had suggested that it make customs entry of them, to take the position that the plaintiff should not

[1] (1886) 18 Q.B.D. 67.

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have paid the duty until the goods were in fact delivered, and ought thus to have attempted to shift to the Crown, if it sought to recover duty, the onus of showing that the missing goods were imported into Canada rather than upon the plaintiff to prove the contrary in order to obtain a refund. It does not, however, appear to me to be necessary to decide this point in the present case since on the evidence the probability appears to me to be that the missing goods were in fact imported into Canada and were lost at some later stage. On this point there is the statement made by Mr. Jewell on discovery, which I regard as an admission by the defendants, that the goods were on board when the ship left Boston which, coupled with the statement that she proceeded therefrom directly to Montreal, appears to me to support the inference and in addition there is the fact that after reporting the goods to the customs authorities as having been imported the defendants, whose responsibility it was to take care of the goods, did not report by an amending declaration nor provide the documentary evidence to establish that they were not in fact imported. There is also the fact, for what it is worth, that their inquiries at other ports at which the ship had called did not indicate that the missing coffee had been landed elsewhere. In my view therefore the missing coffee must be taken to have been imported into Canada and it follows from this that the plaintiff became and was liable to pay the duty thereon notwithstanding that the coffee was never delivered to it. It also follows, in my opinion, that the amount of the duty forms part of the plaintiff's loss flowing from the defendant's failure to deliver the coffee.

The only case cited on this question was that of *Town of Weston v. The Steamer Riverton*[2] where Maclennan L.J.A. said at page 72:

> The plaintiff includes in its action claims for duty, wharfage and handling charges on the shortage. Duty was paid to the Canadian Customs on the bill of lading quantity before the cargo was discharged and before the shortage in delivery was discovered. As soon, however, as the shortage was known it appears to me that the plaintiff was entitled to claim a refund of the duty paid on the shortage. That claim would be against the Customs authorities and cannot be maintained against the ship. The same observations apply to any overcharge made to plaintiff for handling and discharging the cargo. If

[2] [1924] Ex. C.R. 65.

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plaintiff paid more than it should have paid, its claim for reimbursement should have been made against the persons, who were employed to discharge the cargo and not against the ship.

It seems clear that on the facts before him Maclennan L.J.A. did not find that the missing coal had been imported into Canada and as the basis of his conclusion seems to be that duty was not in fact payable in respect of the missing coal the case is distinguishable on its facts from the present. Though the point was conceded rather than decided in favor of the cargo owners in *S.S. Ardennes (Cargo Owners) v. S.S. Ardennes (Owners)*[3] the situation in that case was, I think, nearer in principle to the present than that in the *Riverton* case. There additional customs duty became payable on a cargo by reason of unwarranted delay in delivery of the goods and the cargo owner recovered the amount as part of his damages.

I conclude, therefore, that the customs duty paid by the plaintiff in this case in respect of the coffee would ordinarily be an element to be taken into account in assessing the defendants' damages for the failure to deliver the coffee. There remains, however, a question whether to take it into account in this case is contrary to the terms of the bill of lading. Clause 13 of the bill of lading provided as follows:

> 13. In case of any loss or damage to or in connection with goods exceeding in actual value $500, lawful money of the United States, per package, or, in case of goods not shipped in packages, per customary freight unit the value of the goods shall be deemed to be $500 per package or per unit, on which basis the freight is adjusted and the carrier's liability in any capacity, if any, shall be determined on a value of $500 per package or per customary freight unit, unless the nature of the goods and a valuation higher than $500 shall have been declared in writing by the shipper upon delivery to the carrier and inserted in this bill of lading and extra freight paid if required; and in such case if the actual value of the goods per package or per customary freight unit shall exceed such declared value, the value shall nevertheless be deemed the declared value and the carrier's liability in any capacity, if any, shall not exceed the declared value. *Whenever less than $500 per package or other freight unit, the value of the goods in the calculation and adjustment of claims shall, to avoid uncertainties and difficulties in fixing value be deemed to be the invoice value, plus freight and insurance if paid, whether any other value be higher or lower.* (Italics added).

Clause 16 further provided:

> 16. This bill of lading shall be construed and the rights of the parties thereunder determined according to the law of the United States.

[3] [1951] 1 K.B. 55.

It was urged on behalf of the plaintiff that Clause 13 was contrary to the provisions of section 3(8) of the *Carriage of Goods by Sea Act* of the United States and, therefore, ineffective and void, and in support of this contention, counsel cited *Holden et al v. The S.S. "Kendall Fish"*, a decision of the United States District Court for the Eastern District of Louisiana[4] and the decision of Sidney Smith J. in *Nabob Foods Ltd. v. The Cape Corso*[5] interpreting a similar provision in the English *Carriage of Goods by Sea Act*, 1924. It was not disputed that the provision referred to would render Clause 13 of the bill of lading ineffective and void if the statute applies, but the preamble makes it clear that the statute applies only to bills of lading or similar documents of title which are evidence of a contract for the carriage of goods by sea "to or from" ports of the United States in foreign trade and it appears to me that whatever the contract for the carriage of these goods from the port of Rio de Janeiro may have been and whatever law might in the United States have been applicable thereto up to November 18, 1964, when the original bill of lading in respect of 500 bags of coffee was surrendered and the two new bills of lading for the carriage of the coffee to Montreal were issued, this being at a time when the ship had not yet reached any port of the United States, the contract of carriage was thereafter no longer one for the carriage of goods "to" or "from" ports of the United States. It follows, in my opinion, that the *Carriage of Goods by Sea Act* of the United States could not of its own force apply to govern the rights of the parties under the bill of lading, and on the material before the Court there is nothing which indicates that the terms expressed in the document are not valid and effective to regulate the rights of the parties as terms of the contract of carriage between them. Moreover, there is, in my opinion, nothing in Clause 1 of the bill of lading which renders Clause 13 and in particular the last sentence thereof ineffective or inapplicable in the present situation. Clause 1, as I read it, provides that the terms of the bill of lading shall govern except to the extent that they may be overridden by the application by its own force of either

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[4] [1967] A.M.C. 327.

[5] [1954] Ex. C.R. 335.

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Thurlow J.

the *Carriage of Goods by Sea Act* of the United States or the *Water Carriage of Goods Act* of Canada, neither of which statutes seems to me to apply. Clause 1 then appears to me to go on to stipulate that when neither of these Acts applies of its own force the carrier is to have the same immunities which they provide when they do apply and certain additional immunities as well. There is also no evidence of any law of the United States which would call for an interpretation of the bill of lading or a measure of damages that would be different from that which would be given under the law of Canada.

In the view I take of the matter, however, Clause 13 and in particular the last sentence thereof, does not serve to relieve the defendants from liability for the customs duty paid by the plaintiff on the undelivered coffee. The clause and the particular sentence as well are undoubtedly concerned with the question of the damages to be paid in cases where goods are lost or damaged, but the sentence in question, which the defendants invoke, in my opinion, does not purport to prescribe the measure of damages where goods have been lost. The word "damages" does not even appear in the sentence. What the sentence appears to me to be intended to do is to provide for the calculation of the value of the lost goods as an element of their owner's damages for their loss by reference to their invoice value (plus the freight and insurance if, but only if, paid) and to substitute the result in the place of the result of a calculation based on the market value of the goods at the port of discharge, and the words "whether any other value be higher or lower" appear to me to refer to such market value, which might have increased or declined during the voyage and be higher or lower than the invoice value plus freight and insurance by the time the goods were due at the port of discharge, or to any other method of calculating the value of the goods as an element of their owner's damages.

The reference to "the value of the goods in the calculation and adjustment of claims" is, however, I think, to be read having regard to what the shipowner was obliged by his contract to do, that is to say, carry the goods to the port of discharge and deliver them there, leaving the payment of customs duty, if any, to their owner. So read, the word "value" in the expression which I have quoted from Clause 13 refers to value which would have had to be taken into account as an element of damages for non-delivery if the goods had been lost at sea or had been destined for a place where no duty was imposed on their owner, and it would cover the same element of damages for failure to deliver in the present case. The clause does not appear to me to touch the question of the right of the plaintiff to have the amount of duty for which it has in the meantime become liable included as well in the calculation of its damages for the failure of the defendants to deliver the goods at Montreal.

The plaintiff will, therefore, have judgment for $6,668.57 representing the cost, insurance and freight items totalling $6,424.09, as to which there is no dispute, and $244.48 representing the duty at 2 cents per pound on 12,224 pounds of coffee not delivered. The plaintiff is also entitled to costs.

BETWEEN:

Toronto 1968 Apr. 17-18

EDGELEY FARMS LIMITED ....APPELLANT;

AND

THE MINISTER OF NATIONAL REVENUE .... RESPONDENT.

Income tax—Company formed to acquire land—Grant of long-term lease with option to buy—Profit from exercise of option and expropriation—Whether business profits.

Appellant company was incorporated in 1959 at the instance of four well-to-do men for the purpose of acquiring a 350-acre farm near Toronto as being a good buy though without any definite plan for realizing its potential value. Appellant operated the farm for a short time and then negotiated a 25-year lease of the land to an arm's length purchaser at a high rent subject to an option to purchase at a high price. In 1962 the lessee exercised the option on some of the land. In 1963 an additional part of the land was expropriated. Appellant made a profit of $23,375 on the 1962 sale and $3,100 on the 1963 expropriation.

Held, appellant was not taxable on these sums. Nothing in the circumstances displaced the conclusions that by granting the lease appellant

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committed itself to holding the land as income-producing property for 25 years and that the option clause in the lease was not a dedication of the land to a trading operation.

M.N.R. v. Valclair Investment Co. [1964] Ex. C.R. 466; *M.N.R. v. Cosmos Inc.* [1964] Ex. C.R. 478, distinguished. *Regal Heights Ltd v. M.N.R.* [1960] Ex. C.R. 902, referred to.

INCOME TAX APPEAL.

Wolfe D. Goodman and *Arnold L. Cader* for appellant.

F. J. Dubrule and *J. M. Halley* for respondent.

JACKETT P. (orally):—This is an appeal from the appellant's assessment under Part I of the *Income Tax Act* for the 1962 and 1963 taxation years. What is involved for 1962 is a profit of $23,375 that the appellant made in that year by selling a part of an area of land that it had purchased in 1959. What is involved for 1963 is a profit of $3,100 that the appellant made as a result of an expropriation of another part of the same area of land. The appellant has been assessed on the basis that these amounts were profits from a "business" within the extended meaning of that word as used in the *Income Tax Act* and the sole question involved in the appeal is whether or not those amounts were properly so classified.

The appellant was incorporated in 1959 to acquire 350 acres of land pursuant to an arrangement that had already been worked out by the four individuals who caused it to be incorporated. The land stood in the apparent path of future development of Metropolitan Toronto and the land was acquired because the appellant's management were of the view that it was a good buy.

No attempt was made before me to support the contention put forward at earlier stages of the matter, and suggested in the notice of appeal to this court, that the property was acquired for the purpose of continuing the farming business carried on on the land by the previous owners.

Clearly, as I have said, the land was acquired because it was a good "buy". Its potential value was obvious. What the appellant would do with it was not decided at the time of acquisition. The incorporators were well to do and could afford to bide their time. What the appellant would do with

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the land would depend on what opportunities presented themselves. I have no doubt that, if the guiding mind of the appellant were to have frankly answered questions at the time of acquisition, he would have agreed that the appellant might itself, at an appropriate time, erect on the land buildings suitable for the developing neighbourhood, with a view to renting them or selling them; he would also have agreed that, if the right opportunity or opportunities arose, the appellant might sell some or all of the property, and he would also have agreed that a really attractive bare land leasing proposal would receive careful consideration by the appellant. In other words, the land was not dedicated at the time of acquisition to any particular use. It might end up as stock-in-trade of a trading business or as the subject of a venture in the nature of trade. It might end up as the site for an income-producing building. It might end up as revenue-producing bare land.

In those circumstances, had the acquisition merely been followed by the 1962 sale, I should have had no doubt that the resultant profit was a profit from a business within the extended meaning of that word as used in the *Income Tax Act*. In effect, the appellant would have dedicated the land, or at least that part of it that it sold, to the carrying on of a trading business or a venture in the nature of trade. The two cases on which the appellant relied in that connection—*Minister of National Revenue v. Valclair Investment Co. Ltd.*[1] and *Minister of National Revenue v. Cosmos Inc.*[2] were decisions on different facts and do not do anything more than apply the ordinary principles that have been applied in a line of cases that are so well known that I need only refer to *Regal Heights Ltd. v. Minister of National Revenue*[3] as an example.

The facts are not, however, that simple. Having carried the farming business on for a short time and having then brought it to an end and liquidated the assets of that business other than the land, the appellant negotiated a twenty-five years lease at a very favourable rent with a person with whom it was dealing at arm's length. If the recital of the circumstances stopped there, I should not have had any

1 [1964] Ex.C.R. 466. 2 [1964] Ex.C.R. 478.
3 [1960] S C R. 902.

difficulty in concluding that, at least for the twenty-five year term of the lease, the appellant had dedicated the land to the role of an income-producing investment.

A further circumstance that created a difficulty in my mind, when I first tried to reach a conclusion as to how the particular profits should be classified, is that the long term lease contains an option clause under which the lessee is entitled, if it so elects, to purchase all or parts of the demised property at a price per acre that is substantially higher than the price paid by the appellant for the land. It was pursuant to this option clause that the appellant made the sale giving rise to the profit that is in issue for 1962.

While, as I say, this clause gave me trouble in trying to resolve the problem, I have not been able to find any basis on which I can use it as a reason for coming to a different conclusion than that that I would have reached if there had been a simple twenty-five year lease without an option clause. So far as the appellant is concerned, it has committed itself, by its demise to the lessee, to holding the land in question as income-producing land for twenty-five years. The option clause in no way constitutes a dedication of the land to a trading operation, nor does it confer on the appellant any means for disposing of the land within the twenty-five year period of the lease. Presumably, it was, as part of the process whereby the terms in the lease that were favourable to the appellant were obtained, that the lessee was granted the option clause.

From the point of view of the appellant's ability to sell the land free of the long term lease, the appellant was in the same position as though the lease contained no option clause. If there were no option clause, the appellant would not have been able to sell all or part of the land free of the lease without the cooperation of the lessee. The appellant was in exactly the same position with the option clause in the lease.

I cannot conceive that a similar option clause in a lease granted by a lessor who acquired land for the sole purpose of holding it for a rental income would turn his land holding operation into a trading "business". If it would not have such an effect in the case of such a person, I can conceive no basis for holding that it would have that effect in the case of a person who acquired the land for an undetermined purpose and subsequently committed himself to holding it for rental under a long term lease.

The situation would have been different if the lease had been a mere device for dictating the terms of a land disposition operation. This might have been the case if the lease had been only part of a larger agreement between the appellant and the lessee. It might well have been a fair inference if the rent were so high in relation to the option price as to constitute a strong incentive for the lessee to exercise its option rights. Other circumstances, if they had existed, might have given rise to the same conclusion. No such circumstances had been assumed by the respondent as a basis for the assessments, or alleged by the respondent in his reply to the notice of appeal, and no such circumstance was put forward by counsel for the respondent in cross-examining the appellant's witness.

My conclusion is, therefore, that the land acquired by the appellant in 1959 was being held by the appellant in 1962 and 1963 for rental income under a long term lease, and that the sale in 1962 and the expropriation in 1963 did not give rise to profits from a "business" within the extended meaning of that word as used in the *Income Tax Act*.

The appeal will therefore be allowed and the assessments referred back to the respondent for re-assessment on the basis that the profits in question are not profits from a business. The appellant will have its costs of the appeal.

Toronto 1968

Apr. 2, 19

BETWEEN:

JACK CUPPEL OELBAUM .... APPELLANT;

AND

THE MINISTER OF NATIONAL REVENUE .... RESPONDENT.

Income tax—Husband and wife—Loan to wife on demand note—Income from loan—Whether loan a transfer of property—Whether husband taxable on wife's income—Income Tax Act, s. 21(1).

In 1961 appellant loaned his wife $150,000 on three interest-free demand notes and was assessed to tax on the wife's income of $2,460 in 1963 from the investment of the borrowed money.

Held, allowing the appeal, the loan was not a transfer of property within the meaning of s. 21(1) of the *Income Tax Act.*

Dunkelman v. M.N.R. [1960] Ex.C.R. 73, followed.

INCOME TAX APPEAL.

Wolfe D. Goodman and *Arnold L. Cader* for appellant.

F. J. Dubrule and *J. M. Halley* for respondent.

JACKETT P. (orally):—This is an appeal from the appellant's assessment under Part I of the *Income Tax Act* for the 1963 taxation year.[1] The sole question raised by the appeal is whether section 21(1) of the *Income Tax Act* operates to require that an amount of $2,460.09 be deemed to be income of the appellant and not of his wife.

The facts can be stated shortly. The appellant is a man of means who, as a widower, was married in 1961 to his present wife who was, prior to their marriage, a widow. In 1963, his wife was asked whether she had funds available for investment through the agency of a lawyer, Maxwell Lewis, and she asked her husband to loan her the money that she needed to make that investment. He thereupon loaned her $150,000. The money was paid to her by cheque and, shortly thereafter, she executed three promis-

[1] By agreement of counsel, an appeal from the appellant's assessment for the 1964 taxation year was not proceeded with at this time, even though it is contained in the same Notice of Appeal as the appeal from the assessment for the 1963 taxation year.

sory notes payable on demand in favour of the appellant, each for $50,000. The loan, which bears no interest, is still outstanding.

With the money so loaned by the appellant to his wife, she made an investment or investments from which she had income for the taxation year 1963 in the sum of $2,460.09.

The question is whether that amount must be deemed to be income of the appellant by reason of section 21(1) of the *Income Tax Act*, which reads as follows:

> 21. (1) Where a person has, on or after August 1, 1917, transferred property, either directly or indirectly, by means of a trust or by any other means whatsoever, to his spouse, or to a person who has since become his spouse, the income for a taxation year from the property or from property substituted therefor shall, during the lifetime of the transferor while he is resident in Canada and the transferee is his spouse, be deemed to be income of the transferor and not of the transferee.

If the appellant had made a gift to his wife of the $150,000, instead of loaning it to her, and if all other facts had been the same, it is clear that section 21(1) would have been applicable to require that the income of his wife from investments acquired with that amount be deemed to be income of the appellant.

The respondent's reply to the Notice of Appeal does raise a question as to whether the appellant really loaned the money to his wife. Paragraph 6 of the Reply reads in part:

> 6. In making the re-assessments complained of, the Respondent acted on the following assumptions:
>
> * * *
>
> (*g*) THAT the three purported notes in the name of the wife of the Appellant as maker, in the total amount of $150,000.00, were never intended by the wife of the Appellant or the Appellant to be promissory notes.

It was not suggested that there is any doubt as to the appellant's honesty in giving evidence before me. I accept his evidence, and, on the basis of that evidence, I find that the $150,000 was *loaned* by the appellant to his wife and was not *given* to her.

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In these circumstances, the question that I have to decide is whether, when a husband has paid money to his wife by way of loan, he can be said to have "transferred property" to her within the meaning of those words as they are used in section 21(1) of the *Income Tax Act.*

Precisely the same question arose in another case in this court in 1959 with reference to the same words as they are used in section 22(1) of the *Income Tax Act,* which reads as follows:

> 22. (1) Where a taxpayer has, since 1930, transferred property to a person who was under 19 years of age, either directly or indirectly by means of a trust or by any other means whatsoever, the income for a taxation year from the property or from property substituted therefore shall, during the lifetime of the taxpayer while he is resident in Canada, be deemed to be income of the taxpayer and not of the transferee unless the transferee has before the end of the year attained the age of 19 years.

In that case there was a loan by the taxpayer to trustees for his minor children. Mr. Justice Thurlow decided—see *Dunkelman v. Minister of National Revenue*[2]—that section 22(1) did not apply because, in the context in which they are used in that provision, the words "has... transferred property" did not apply to a loan transaction. At pages 81-2, he said:

> I do not think it can be denied that, by loaning money to the trustees, the appellant, in the technical sense, transferred money to them, even though he acquired in return a right to repayment of a like sum with interest and a mortgage on the Butterfield Block as security, or even though he has since then been repaid with interest. But, in my opinion, it requires an unusual and unnatural use of the words "has transferred property" to include the making of this loan. For who, having borrowed money and knowing he must repay it, would use such an expression to describe what the lender has done? Or what lender thinks or speaks of having transferred his property, when what he has done is to lend it? Or again, what casual observer would say that the lender, by lending, "has transferred property"? And, more particularly, who would so describe the lending where, as in this case, the transaction is such that the only purpose to which the money loaned could be turned was in acquiring a property to be immediately mortgaged to the lender? I venture to think, in the terms used by Lord Simonds, that no one, be he lawyer, business man, or man in the street, uses such language to describe such an

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[2] [1960] Ex.C.R. 73.

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> act. I also think that, if Parliament had intended to include a loan transaction such as the present one, the words necessary to make that intention clear would have been added, and it would not have been left to an expression which, in its usual and natural meaning, does not clearly include such a transaction. To apply the test used by Lord Simonds, I do not think this transaction was one which the language of the subsection, according to its natural meaning, "fairly" or "squarely" hits. I am, accordingly, of the opinion that the making of the loan in question was not a transaction within the meaning of the expression "has transferred property" and that s. 22(1) does not apply.

With that reasoning, with respect, I entirely agree, and I think it applies equally to the interpretation of section 21(1). Counsel for the respondent agreed that the reasoning in the *Dunkelman* decision applies to section 21(1) just as much as it does to section 22(1), but contended that it only applies where there was a more business like transaction than there is in the case at bar. He relied on the fact that, in the *Dunkelman* case, there was a mortgage to the tax-payer by way of security for his loan and contended that that made the facts distinguishable from this case where there is no written record of the loan except promissory notes. With all respect to that submission, I cannot see any possible distinction, from the point of view of the reasoning in the *Dunkelman* case, between the facts in that case and the facts in the present appeal.

The appeal is allowed with costs, and the appellant's assessment under Part I of the *Income Tax Act* for the 1963 taxation year is referred back to the respondent for re-assessment on the basis that section 21(1) does not apply to the income of $2,460.09 from the appellant's wife's investments.

Montreal 1968

March 8

Ottawa April 5

CITIZENSHIP APPEAL COURT

IN THE MATTER OF Elise Dervishian ....APPELLANT.

Citizenship—Appeal from rejection of application—Whether applicant "of good character" or "de bonne vie et moeurs"—Conviction of criminal offence—Whether proof of rehabilitation—Citizenship Act, s. (10)(1)(d).

The question whether an applicant for citizenship is "of good character" or "de bonne vie et moeurs" within the meaning of s. 10(1)(*d*) of the *Citizenship Act* must be considered as of the time the court is considering the matter, and an applicant who has been convicted of a criminal offence is entitled to a finding that he is of good character when he has satisfied the sentence imposed and demonstrated by his subsequent conduct and way of life that he has rehabilitated himself. The matter must be considered from the point of view of the seriousness of the offence on the one hand and of the length of the period during which he has been living the life of a law-abiding and useful member of society on the other. As a general rule the applicant should bring before the court some unrelated person or persons able to testify as to the type of life he has been living since he satisfied the sentence

APPEAL from decision of Citizenship Court, Montreal.

Jacques Bellemare amicus curiae.

THE COURT (Jackett, Dumoulin, Noël JJ.):—This appeal was heard at the same time as three other appeals[1] because, in each case, the application for citizenship was rejected by the Citizenship Court after it came to the conclusion that the appellant did not have a "good character" within the meaning of section 10(1)(*d*) of the *Citizenship Act*, apparently by reason of the fact that the appellant had been convicted of one or more offences under the Criminal Code.

Having regard to the importance of establishing, as far as this Court is concerned, how such a problem should be resolved, the Court requested the appointment of an *amicus curiae* for each of the four appeals and, as a result, Mr. Jacques Bellemare of Montreal acted in that capacity and has been of great assistance to the Court.

The appellant, Elise Dervishian, was born in Nicosia, Cyprus, on January 28, 1923, and came to Canada on July 10, 1962. On October 31, 1963, she was convicted of petty

[1] Not reported.

theft and was fined $25. The record shows that she was convicted of stealing a dressing gown, two pairs of gloves, and a bottle of toilet water from Steinberg Ltd. The appellant is married and lives in Montreal with her husband and children. The decision of the Court appealed from in this case was rendered on July 25, 1967, and reads:

1968 *In re* ELISE DERVISHIAN — Jackett J. Dumoulin J. Noël J.

> The petitioner, Elise Dervishian, made on April 12, 1967, an application under Section 10 (1) of the *Canadian Citizenship Act*.
>
> At the hearing, the applicant admitted that she has been convicted for shoplifting on December 30, 1965, and condemned in Montreal to pay $20.00 or $25 00 fine.
>
> The Court concludes that the applicant does not meet the requirements of the law, as provided under Section 10(1)(*d*) of the Act.
>
> The petition is rejected.

Section 10(1) of the *Citizenship Act* authorizes the "Minister" to grant a certificate of citizenship to any person who is not a Canadian citizen and who makes application for such a certificate if that person satisfies the "Court" as to the various matters therein set out. We are here concerned with the requirement set out in the first part of paragraph (*d*) of section 10(1) of the English version of the statute, which is that the applicant satisfy the Court that "he is of good character". While paragraph (*d*) was re-enacted by chapter 4 of the Statutes of 1967, which came into force on July 7, 1967, those words remain unchanged in the revised paragraph. The corresponding words in the French version of paragraph (*d*) before July 7, 1967, were "qu'elle a une bonne moralité", and since that day are "qu'elle est de bonne vie et moeurs".

What the Court must keep in mind in applying the requirement that an applicant be "of good character" or "de bonne vie et moeurs" is that the question must be considered with reference to the time that the Court has the matter under consideration. While, therefore, one might be forced to conclude that a person would have been unable to show that he was of good character at the time that he was convicted of a serious criminal offence, it does not follow that such a conviction prevents him from satisfying a court as to his good character at some subsequent time.

Our view is that, after a person who has been convicted of a criminal offence has served any term of imprisonment

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In re ELISE DERVISHIAN

Jackett J. Dumoulin J. Noël J.

that has been imposed on him or has otherwise satisfied any sentence that has been passed on him in respect of his offence, and after he has demonstrated by his subsequent course of conduct and way of life that he has rehabilitated himself in the eyes of right thinking citizens, he is entitled to a finding that he is of good character within the meaning of section 10(1)(*d*).

While there can be no rule of thumb for the decision of such matters, as it appears to us, the matter must be considered from the point of view of the seriousness of the offence of which he has been convicted, on the one hand, and of the length of the period during which he has been living the life of a law-abiding and useful member of society on the other hand.

As a general rule, we should have thought, in a case where an applicant has had a criminal conviction at some time in his past, he should be expected to bring before the court of first instance some unrelated person or persons able to testify as to the type of life that he has been living since the time when he finished his prison sentence or otherwise complied with the sentence imposed on him.

In this case, this was not done and this Court has, therefore, given special attention to the story told to the Court by the appellant herself and her husband, and to the manner in which the story was told. We have been impressed by the way in which the appellant has told her story and we are satisfied that the appellant has learned whatever lesson should have been learned from her brush with the law, and is endeavouring, with considerable success, to lead a good and useful life. In the sense in which the word is used in connection with penal matters, we are satisfied that the appellant has been "rehabilitated". Our view is, therefore, that we should make a finding that the appellant is of good character, or "de bonne vie et moeurs".

Before leaving the matter, there is a comment of general interest in connection with applications for citizenship under section 10(1) of the *Citizenship Act,* which should be made. Under section 5 of the Rules of this Court, upon an appeal being launched to this Court, the court of first instance and the Minister are to forward to this Court all relevant files and information. In none of the appeals that have been launched prior to this time and that have come to our attention has there been any material to indicate that any inquiries have been made, by any person representing the public interest, concerning the accuracy of the information set out by the appellant in his application form. It would seem, therefore, that the court of first instance has been left in each case to deal with an application on the statements put before the Court by the applicant. In this case, the appellant has made honest replies to the inquiries concerning her criminal record. If the appellant had not revealed that record, we can only assume that the Court would have known nothing about it. If the granting of Canadian citizenship is a matter of such importance to the nation as we deem it to be, we should have thought that it warrants some system whereby some check is made on an applicant's statements concerning the conditions laid down by Parliament to the granting of Canadian citizenship. In the case of immigration status and criminal records at least, we should have thought that there are obvious inquiries that could be made without undue difficulty or delay. With reference to immigration status, it should be possible to obtain, and place before the court of first instance, a statement from the appropriate immigration authority as to the accuracy of the statements in the application. With reference to criminal records, it should be possible to obtain, in each case, a certificate as to whether the applicant has a criminal record or not, and, if he has one, an authentic statement as to the charges of which the applicant has been convicted. In addition we suggest that, where practicable, it would be very helpful to the court of first instance to have a recommendation from the judge who pronounced the conviction concerning the applicant's application for citizenship.

Montreal 1968

May 7

CITIZENSHIP APPEAL COURT

IN THE MATTER OF Teodora Albrecht ....APPELLANT.

Citizenship—Appeal from rejection of application—Intention to have permanent domicile in Canada—Relevant time of intention, whether date of application or hearing—Citizenship Act, s. 10(1)(g).

Citizenship—Appeal—Necessity of proof of requirements of s. 10(1) to satisfaction of appeal court.

An intention to have one's place of domicile permanently in Canada, which is required of an applicant for citizenship under s. 10(1)(*g*) of the *Citizenship Act,* must exist to the satisfaction of the court dealing with the matter at the time of the court's decision, not at the time of the application for citizenship.

Semble. An appeal from a decision of a citizenship court is a new trial and before reversing that decision the appellate court must be satisfied that the applicant has fulfilled *all* the requirements of s. 10(1) of the *Citizenship Act* and not merely the particular requirement or requirements as to which the court below was not satisfied.

APPEAL from decision of Citizenship Court, Montreal.

A. H. J. Zaitlin, Q.C. for appellant.

JACKETT J. (orally):—This is an appeal from a decision of the Court of Canadian Citizenship, Montreal, deciding that the appellant is not a fit and proper person to be granted Canadian citizenship.

The appellant satisfied the Court from whose decision the appeal was taken concerning all the requirements of subsection (1) of section 10 of the *Citizenship Act,* except the requirement contained in paragraph (*g*) thereof which is that an applicant for Canadian citizenship "intends to have his place of domicile permanently in Canada".

The appellant has been represented in this Court by counsel who submitted, in effect, that all that this Court has to do in such a case is make a finding with regard to the requirement concerning which the appellant failed before the Court of first instance. I am inclined to the view that, if this Court reverses the decision of the Court of first instance, it must also give a judgment that it is satisfied, in effect, as to all the matters detailed in section 10(1), as such a decision by a court is a condition precedent to the granting to the appellant of a certificate of citizenship by the Minister. In this case, however, I am satisfied by the evidence given before me concerning all the requirements of section 10(1) upon which the Court of first instance appears to have been satisfied, so that it is not necessary for me to come to a final conclusion on the question whether an appeal to this Court is a "new trial" of the whole of the application. I must say, however, that, as I presently view the matter, an appeal to this Court is such a new trial.

Turning to the question on which the Court of first instance rejected the application, I refer first to the reasons given by that Court, which read as follows:

> The petitioner, Teodora Albreht, (*sic*) made on September 29, 1967, an application under Section 10(1) of the *Canadian Citizenship Act*.
>
> When filing her application, she answered to question 14: "Yes, but I would like to travel".
>
> At the hearing of the petition before the Court on December 29, 1967, the petitioner said: "I intend to go to my country to visit and if I have possibility to live there all the time, I would stay".
>
> The Court tried to ask her if she wanted to stay in her mother country for six months or one year, she did not answer.
>
> Considering that the applicant does not intend to have her place of domicile in Canada;
>
> Under the circumstances, the Court has to reject the petition under Section 10(1)(*g*) of the *Canadian Citizenship Act*.
>
> The Court rejects the petition.

The requirement in section 10(1)(*g*) is, as I have already indicated, that the applicant "intends to have her place of domicile permanently in Canada". Counsel submitted that this intention must relate to the time of the application. In my view, it must be an intention that exists to the satisfaction of the Court dealing with the matter at the time that it gives its decision.

If the only evidence before me were the statement of the appellant contained in the judgment appealed from that, if she had a possibility of staying in her country, by which she meant Yugoslavia, she would stay there, I doubt that I could render a decision that I am satisfied that she intends to have her place of domicile permanently in Canada.

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I would find it hard to be satisfied that a person who said that had presently an intention to make his or her home permanently in Canada.

Unfortunately, we have no record in this case of what other evidence was before the Court of first instance or of the reasons why her application for naturalization in 1963 was rejected.

On the other hand, I have had the advantage of hearing the appellant testify before me under oath and I am of opinion that she was an honest witness.

She testified before me, in effect, that she regards Canada as her permanent home and has no thought of going anywhere else to live. She says that her mother is in Yugoslavia and that she would like, if it were ever possible, to visit her mother there. She explains the statement that she made before the Court of first instance as having been given when she was very nervous. She tells me, in effect, and I believe her, that regardless of what she said in her nervousness she has, since 1951, made her home in Montreal and has no plan or desire to go and live somewhere else.

In the circumstances, I am satisfied although I have no difficulty in appreciating why the Court of first instance was not, that the appellant intends to have her place of domicile permanently in Canada.

The decision appealed from is reversed and it is declared that the Court is satisfied that the appellant is a fit and proper person to be granted Canadian citizenship under section 10(1) of the *Citizenship Act*.

CITIZENSHIP APPEAL COURT

Kamloops
1968
June 7
Ottawa
June 19

IN THE MATTER OF Bjarne Almaas ......APPELLANT;

IN THE MATTER OF Edith Almaas ......APPELLANT;

IN THE MATTER OF Egon Nielsen ....APPELLANT;

IN THE MATTER OF Teresa Nielsen ......APPELLANT.

Citizenship—Appeal from rejection of application—Conscientious objection to serving in armed forces and voting in elections—Whether disqualification for citizenship—Citizenship Act, s. 10(1)(f).

Neither section 10(1)(*f*) of the *Citizenship Act* nor the oath of allegiance which an applicant for citizenship must take requires a willingness to serve in Canada's armed forces if lawfully called upon as a qualification for citizenship, and hence an applicant's objection upon religious grounds to serve in the armed forces of Canada does not disqualify him for citizenship nor preclude the court from being satisfied of his qualifications under s. 10(1) of the Act.

For similar reasons an applicant's objection upon religious grounds to voting in elections for public office neither disqualifies him for citizenship nor precludes the court from being satisfied of his qualifications under s. 10(1) of the Act.

United States v. Schwimmer 279 U.S. 644;
United States v. Macintosh 283 U.S. 605;
United States v. Bland 283 U.S. 636;
Girouard v. United States 328 U.S. 61, considered.

APPEALS from decisions of County Court of Yale, B.C.

K. D. Houghton amicus curiae.

KERR J.:—These appeals are in respect of four applications for Canadian citizenship which were heard by the County Court of Yale, British Columbia, under the provisions of the *Canadian Citizenship Act*. In each case the County Court decided that, because the applicant therein is a conscientious objector against serving in the military forces of Canada, it was not satisfied to recommend to the Secretary of State for Canada that the applicant be granted a certificate of Canadian citizenship. All four applicants appealed to this Court and the appeals were heard at Kamloops, British Columbia, on June 7, 1968.

As the general issues are the predominant features and are similar in all cases and as the facts may be briefly stated and are not in dispute, it is convenient to give one set of reasons for my disposition of the four appeals.

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Each appellant appeared in person at the hearing of the appeals and testified under oath. None was represented by counsel. The Court requested the appointment of an *amicus curiae* for each of the appeals and Mr. K. D. Houghton, Barrister of Kamloops, acted in that capacity and was of great assistance to the Court.

The general issues in all cases are the conscientious objections of the appellants to serving in the armed services of Canada and to voting in elections for public office. The latter objection was disclosed by the appellants during the hearing of the appeals when they were questioned concerning their knowledge of the responsibilities and privileges of Canadian citizenship and their willingness to take the oath of allegiance set out in the Second Schedule to the *Canadian Citizenship Act* and their intention to comply with it. All the appellants belong to the religious body known as "Jehovah's Witnesses".

The appellant, Bjarne Almaas, is a married man, carpenter by occupation, who was born in Norway in 1915, was lawfully admitted to Canada for permanent residence in 1957 and has lived in Enderby, B.C., ever since that time. His wife, Edith Almaas, was born in Norway in 1918, was lawfully admitted to Canada in 1957 for permanent residence and has lived in Enderby, B.C., ever since then. Mr. and Mrs. Almaas have three children, two of whom are under 21 years of age and live in Enderby, the third is just over 21 years old and lives in Vernon, B.C.

The appellant, Egon Nielsen, is a married man, carpenter by occupation, who was born in Denmark in 1922, was lawfully admitted to Canada for permanent residence in 1951 and has lived in Ontario and British Columbia since that time. His wife, Teresa Nielsen, is also an appellant. She was born in Denmark in 1923, was lawfully admitted to Canada for permanent residence in 1951 and has lived in Ontario and British Columbia ever since. Mr. and Mrs. Nielsen have two children who were born in Canada.

All the appellants speak English very well and impressed me favourably. In my opinion, each one is of good character and satisfies the other requirements of section 10(1) of the *Citizenship Act*. I will deal specifically with the conscientious objections of the appellants, as these appeals are the first in this Court in which such objections have been considered.

Section 10(1) of the Act authorizes the "Minister" to grant a certificate of citizenship to any person who is not a Canadian citizen and who makes application for such a certificate if that person satisfies the "Court" as to the various matters set out therein. The Court is concerned in relation to these appeals particularly with the requirement set out in paragraph (*f*) of section 10(1), which is that the applicant satisfy the court that "he has an adequate knowledge of the responsibilities and privileges of Canadian citizenship and intends to comply with the oath of allegiance set forth in the Second Schedule".

The Oath of Allegiance is as follows:

> I, A B, swear that I will be faithful and bear true allegiance to Her Majesty Queen Elizabeth the Second, her Heirs and Successors, according to law, and that I will faithfully observe the laws of Canada and fulfil my duties as a Canadian citizen.
>
> So help me God.

Section 33 of the Act provides that the Court shall impress upon the applicants the responsibilities and privileges of Canadian citizenship.

Each of the appellants expressed a willingness to take the oath of allegiance. Their objections to serving in the armed services and to voting are based on their convictions as to what the Bible teaches and as to what God's laws and arrangements for the human race are. They believe that "His will" will eventually come about. They are willing to serve Canada as good citizens and obey the laws of Canada, subject to the reservation that they regard what they believe to be God's laws as supreme and superior to man-made laws and in the event of conflict between the two kinds of laws, they will feel bound to obey God's laws.

Somewhat similar situations involving applicants for United States citizenship who had conscientious objections against serving in the armed forces of that country were the subject of consideration by the Supreme Court of the United States. I will quote from the decisions given by the Justices of that Court to indicate the views held by eminent

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jurists and the arguments that can be offered in favour of and against the granting of Canadian citizenship to persons who have conscientious objections such as are under consideration here.

The first case was *United States v. Schwimmer*[1], in which the Supreme Court refused citizenship to a woman who said that she was a conscientious objector and would not take up arms in defence of her country. As a condition precedent to a grant of citizenship the applicable statute law of the United States required the applicant to take an oath of allegiance which included a declaration that the applicant "will support and defend the Constitution and laws of the United States against all enemies, foreign and domestic, and bear true faith and allegiance to the same". In its decision the Supreme Court said, *inter alia*:

> That it is the duty of citizens by force of arms to defend our government against all enemies whenever necessity arises is a fundamental principle of the Constitution.
>
> The common defense was one of the purposes for which the people ordained and established the Constitution. ... We need not refer to the numerous statutes that contemplate defense of the United States, its Constitution and laws by armed citizens. This Court, in the *Selective Draft Law Cases*, 245 U.S. 366, speaking through Chief Justice White, said (p. 378) that "the very conception of a just government and its duty to the citizen includes the reciprocal obligation of the citizen to render military service in case of need. ..."
>
> Whatever tends to lessen the willingness of citizens to discharge their duty to bear arms in the country's defense detracts from the strength and safety of the Government. And their opinions and beliefs as well as their behavior indicating a disposition to hinder in the performance of that duty are subjects of inquiry under the statutory provisions governing naturalization and are of vital importance, for if all or a large number of citizens oppose such defense the "good order and happiness" of the United States can not long endure. And it is evident that the views of applicants for naturalization in respect of such matters may not be disregarded. The influence of conscientious objectors against the use of military force in defense of the principles of our Government is apt to be more detrimental than their mere refusal to bear arms. The fact that, by reason of sex, age or other cause, they may be unfit to serve does not lessen their purpose or power to influence others.

Mr. Justice Holmes delivered a dissenting opinion which was concurred in by Mr. Justice Brandeis.

[1] 279 U.S. 644 at p. 650.

The matter came before the Supreme Court of the United States again in 1930 in *United States v. Macintosh*[2], in which the Court refused citizenship to an applicant who was unwilling to take the oath of allegiance except with certain reservations, one of which was that he would not assist in the defence of the United States by force of arms or give any war his moral support unless he believed it to be morally justified. I quote the following excerpts from the ruling opinion of the majority of the Court:

> When he speaks of putting his allegiance to the will of God above his allegiance to the government, it is evident, in the light of his entire statement, that he means to make *his own interpretation* of the will of God the decisive test which shall conclude the government and stay its hand. We are a Christian people (*Holy Trinity Church v. United States,* 143 U.S. 457, 470-471), according to one another the equal right of religious freedom, and acknowledging with reverence the duty of obedience to the will of God. But, also, we are a Nation with the duty to survive; a Nation whose Constitution contemplates war as well as peace; whose government must go forward upon the assumption, and safely can proceed upon no other, that unqualified allegiance to the Nation and submission and obedience to the laws of the land, as well those made for war as those made for peace, are not inconsistent with the will of God.
>
> . . .
>
> . . . As this Court said in *United States v. Manzi,* 276 U.S. 463, 467: "Citizenship is a high privilege, and when doubts exist concerning a grant of it, generally at least, they should be resolved in favor of the United States and against the claimant."
>
> The *Naturalization Act* is to be construed "with definite purpose to favor and support the Government," and the United States is entitled to the benefit of any doubt which remains in the mind of the court as to any essential matter of fact. The burden was upon the applicant to show that his views were not opposed to "the principle that it is a duty of citizenship, by force of arms when necessary, to defend the country against all enemies, and that (his) opinions and beliefs would not prevent or impair the true faith and allegiance required by the Act." *United States v. Schwimmer, supra,* 649, 650, 653. We are of opinion that he did not meet this requirement.

In the *Macintosh* case Chief Justice Hughes wrote a dissenting opinion, with which Justices Holmes, Brandeis and Stone concurred, which included the following statements at pp. 627, 629-30, 632 & 633-34:

> . . . The question is not whether naturalization is a privilege to be granted or withheld. That it is such a privilege is undisputed. Nor, whether the Congress has the power to fix the conditions upon which

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[2] 283 U.S. 605 at pp. 625 & 626.

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the privilege is granted. That power is assumed. Nor, whether the Congress may in its discretion compel service in the army in time of war or punish the refusal to serve. That power is not here in dispute. Nor is the question one of the authority of Congress to exact a promise to bear arms as a condition of its grant of naturalization. That authority, for the present purpose, may also be assumed.

The question before the Court is the narrower one whether the Congress has exacted such a promise.

. . .

. . . He declared that "his first allegiance was to the will of God"; that he was ready to give to the United States "all the allegiance he ever had given or ever could give to any country, but that he could not put allegiance to the Government of any country before allegiance to the will of God". The question then is whether the terms of the oath are to be taken as necessarily implying an assurance of willingness to bear arms, so that one whose conscientious convictions or belief of supreme allegiance to the will of God will not permit him to make such an absolute promise, cannot take the oath and hence is disqualified for admission to citizenship.

. . .

The question of the proper interpretation of the oath is, as I have said, distinct from that of legislative policy in exacting military service. The latter is not dependent upon the former. But the long-established practice of excusing from military service those whose religious convictions oppose it confirms the view that the Congress in the terms of the oath did not intend to require a promise to give such service. The policy of granting exemptions in such cases has been followed from colonial times and is abundantly shown by the provisions of colonial and state statutes, of state constitutions, and of acts of Congress.

. . .

Much has been said of the paramount duty to the State, a duty to be recognized, it is urged, even though it conflicts with convictions of duty to God. Undoubtedly that duty to the State exists within the domain of power, for government may enforce obedience to laws regardless of scruples. When one's belief collides with the power of the State, the latter is supreme within its sphere and submission or punishment follows. But, in the forum of conscience, duty to a moral power higher than the State has always been maintained. The reservation of that supreme obligation, as a matter of principle, would unquestionably be made by many of our conscientious and law-abiding citizens. The essence of religion is belief in a relation to God involving duties superior to those arising from any human relation.

. . .

. . . The battle for religious liberty has been fought and won with respect to religious beliefs and practices, which are not in conflict with good order, upon the very ground of the supremacy of conscience within its proper field. What that field is, under our system of government, presents in part a question of constitutional law and also, in part, one of legislative policy in avoiding unnecessary clashes with the dictates of conscience. There is abundant room for enforcing the requisite authority of law as it is enacted and requires obedience, and for maintaining the conception of the supremacy of law as essential to orderly government, without demanding that either citizens or applicants for citizenship shall assume by oath an obligation to regard allegiance to God as subordinate to allegiance to civil power.

In 1931 the matter once again came before the Supreme Court in *United States v. Bland*[3] and the Court followed the majority decision in the *Macintosh* case.

Finally in 1946, the Supreme Court of the United States reviewed the question in *Girouard v. United States*[4]. In this case the applicant was willing to take the oath of allegiance but to the question "If necessary, are you willing to take up arms in defence of this country?" he replied, "No (Non-combatant) Seventh Day Adventist", and explained that it was a purely religious matter with him. The Supreme Court this time held that the rule in the *Schwimmer, Macintosh* and *Bland* cases that an alien who refused to bear arms will not be admitted to citizenship was fallacious and the Court overruled those previous decisions. Following are excerpts from the decision:

The oath required of aliens does not in terms require that they promise to bear arms. Nor has Congress expressly made any such finding a prerequisite to citizenship. To hold that it is required is to read it into the Act by implication. But we could not assume that Congress intended to make such an abrupt and radical departure from our traditions unless it spoke in unequivocal terms.

The bearing of arms, important as it is, is not the only way in which our institutions may be supported and defended, even in times of great peril. Total war in its modern form dramatizes as never before the great cooperative effort necessary for victory. The nuclear physicists who developed the atomic bomb, the worker at his lathe, the seamen on cargo vessels, construction battalions, nurses, engineers, litter bearers, doctors, chaplains—these, too, made essential contributions. And many of them made the supreme sacrifice. Mr. Justice Holmes stated in the *Schwimmer case* (279 U.S. p. 655) that "the Quakers have done their share to make the country what it is." And the annals of the recent war show that many whose religious scruples prevented them from bearing arms, nevertheless were unselfish participants in the war effort. Refusal to bear arms is not necessarily a sign of disloyalty or a lack of attachment to our institutions. One

[3] 283 U.S. 636.

[4] 328 U.S. 61 at pp. 64-5, 68 & 69.

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may serve his country faithfully and devotedly, though his religious scruples make it impossible for him to shoulder a rifle. Devotion to one's country can be as real and as enduring among non-combatants as among combatants. One may adhere to what he deems to be his obligation to God and yet assume all military risks to secure victory. The effort of war is indivisible; and those whose religious scruples prevent them from killing are no less patriots than those whose special traits or handicaps result in their assignment to duties far behind the fighting front. Each is making the utmost contribution according to his capacity. The fact that his rôle may be limited by religious convictions rather than by physical characteristics has no necessary bearing on his attachment to his country or on his willingness to support and defend it to his utmost.

. . .

Mr. Justice Holmes stated in the *Schwimmer* case (279 U.S. pp. 654-55): "if there is any principle of the Constitution that more imperatively calls for attachment than any other it is the principle of free thought—not free thought for those who agree with us but freedom for the thought that we hate. I think that we should adhere to that principle with regard to admission into, as well as to life within this country." The struggle for religious liberty has through the centuries been an effort to accommodate the demands of the State to the conscience of the individual. The victory for freedom of thought recorded in our Bill of Rights recognizes that in the domain of conscience there is a moral power higher than the State. Throughout the ages, men have suffered death rather than subordinate their allegiance to God to the authority of the State. Freedom of religion guaranteed by the First Amendment is the product of that struggle.

. . .

We conclude that the *Schwimmer, Macintosh* and *Bland* cases do not state the correct rule of law.

In considering in connection with the appeals before this Court the decisions of the Supreme Court of the United States one must bear in mind that they relate to the laws of that country and that the qualifications for citizenship and the form of the oath of allegiance there are expressed differently from the corresponding qualifications and oath of allegiance in Canada; but I do not think that there is a significant difference in the principles and the concept of good citizenship upon which the respective laws are based.

In Canada, as in the United States, the right of an alien to acquire citizenship is purely statutory. An applicant must first satisfy the court that he has the qualifications set out in section 10(1) of the *Canadian Citizenship Act* and he must be willing to take, and must intend to comply with, the oath of allegiance. The relevant paragraph (*f*) of subsection (1) of section 10 and the oath of allegiance are expressed in general words. They do not expressly set out, as a qualification for acquiring Canadian citizenship, a willingness to serve in the armed forces of Canada if lawfully called upon to do so, nor do they require an undertaking to do so. Service in the Canadian armed forces has traditionally been on a voluntary basis. Compulsory military service has not generally been resorted to. Of course, Parliament has legislative authority to enact laws requiring persons to serve in the armed forces and has authority to impose penalties for failure to comply with such laws. Canada also has power to prescribe the qualifications that an alien must have in order to acquire citizenship; and if the *Canadian Citizenship Act* were to set out, as one of those qualifications, a willingness on the part of the applicant to serve in Canada's armed forces if lawfully called upon to do so, or if the Act were to require an undertaking to do so, the court would have no alternative but to apply the law. However, I do not construe the Act or the oath of allegiance as containing such a qualification or requirement, either expressly or by necessary implication.

The Parliament of Canada has affirmed, in the preamble to Part I, the *Bill of Rights,* chapter 44 of the 1960 statutes, that the Canadian nation is founded upon principles that acknowledge the supremacy of God, the dignity and worth of the human person and the position of the family in a society of free men and free institutions and has also affirmed that men and institutions remain free only when freedom is founded upon respect for moral and spiritual values and the rule of law.

It is beyond dispute that persons who refuse to serve in the armed forces because of religious beliefs may still serve Canada well in other ways in peace and in war. They can be good citizens, notwithstanding their refusal to serve in the armed forces.

I find that the expressed unwillingness of the appellants to serve in the armed forces of Canada does not disqualify them from acquiring Canadian citizenship and does not

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preclude the Court from being satisfied as to the various matters set out in section 10(1) of the *Canadian Citizenship Act* insofar as the appellants are concerned.

Now, as to the other objection of the appellants against voting in elections for public office. This objection is also based upon religious and conscientious convictions held by them. They are unwilling to take part, by voting, in the process by which the Members of Parliament and other legislative bodies are elected. The franchise, the right to vote, is an essential feature of our democratic system of Government. People are urged to vote and are told that it is their duty to do so. Our system would falter if most qualified voters refused to vote. However, the right to vote is a privilege that many good Canadian citizens choose from time to time not to exercise, for one reason or another, even for reasons less compelling than religious convictions. I would not regard the refusal of the appellants to vote as a failure on their part to discharge their duty as citizens. As in the case of the objection to military service, and for similar reasons, I find that the objection of the appellants, on religious grounds, to voting and their intention not to vote do not disqualify them from becoming Canadian citizens and do not preclude the Court from being satisfied as to the matters set out in section 10(1) of the Act. As already stated, my opinion is that each of the appellants is of good character and satisfies the requirements of section 10(1).

The decisions appealed from are reversed and it is declared that this Court is satisfied that each of the appellants, Bjarne Almaas, Edith Almaas, Egon Nielsen and Teresa Nielsen, is a fit and proper person to be granted Canadian citizenship under section 10(1) of the *Canadian Citizenship Act*.

BETWEEN:

LAKE LOUISE SKI LODGE LIMITED, ALFRED COOPER and MARY BOYLE .... SUPPLIANTS;

Calgary 1967

March 29–31 Apr. 3–7

Ottawa Apr. 25

AND

HER MAJESTY THE QUEEN............RESPONDENT.

Expropriation—Crown—Agreement to compensate subject—Exchequer Court Act, R.S.C. 1952, c. 98, s. 18(1)(g)—Concept of "value to the owner"—Subject property—No value beyond "market value"—Sole criteria was "market value" at the date of the expropriation.

The respondent expropriated on the 2nd of August 1956 certain parcels of lands in the Lower Lake Louise area in Banff National Park, Alberta, of which the suppliants were the owners prior thereto.

The suppliants sought to establish that their claim for compensation arising out of their expropriation should be based on the concept of "value to the owner"; and adduced evidence through expert witnesses, *inter alia,* of a possible substantial development on the subject lands.

The respondent sought to establish that the subject property had no value beyond "market value".

Held, on the evidence that there was proof that there was a market for the subject properties, but there was no proof given of any special adaptability or use of any of the subject properties and therefore there was no special value to the suppliants within the meaning of the decided cases and as a consequence "market value" was the sole criteria of the values of the subject properties as of the date of the expropriation.

Held also, that the evidence of certain expert witnesses in this case, who prepared certain grandiose possible schemes of development for the main parcel of the subject properties, had little or no weight for the purpose of this adjudication of the compensation payable, because such schemes of development were not factors in the market at the date of expropriation.

EXPROPRIATION.

E. M. Woolliams, Q.C. and *D. G. Korman* for suppliants.

Ross A. MacKimmie, Q.C. and *P. M. Troop* for respondent.

GIBSON J.:—The suppliants in this action claim damages against the respondent arising out of an expropriation on the 2nd of August, 1956 of certain lands in the Lower Lake Louise area in Banff National Park, Alberta.

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The respective subject lands formerly owned by the supplants were as follows, *viz*:

1. J. Stanley Boyle was the owner of a triangular piece of land located on the north side of the Banff Jasper Highway about 500 feet west of the original road allowance between sections 27 and 28 having frontage of approximately 600 feet and an area of approximately 2.0 acres. (This is referred to and identified as parcel B on Exhibit S-8 and on the plan attached to Exhibit R-5.)

2. Alfred Cooper was the owner of a piece of land adjoining and it also fronts on the Banff Jasper Highway and its easterly boundary is formed by the original road allowance between sections 27 and 28 and its highway frontage is approximately 650 feet and it has an area of approximately 4.40 acres. (This property is referred to and identified as parcel C on Exhibit S-8 and on the plan attached to Exhibit R-5.)

3. Lake Louise Ski Lodge Limited was the owner of two parcels of land, that is to say:

   One parcel (which is the principal parcel) consisted of an irregular area bounded on the north and west by Pipestone Creek and on the south by the Canadian Pacific Railway. A tongue of land 40 feet wide on the western limit of the property extends west from across the Pipestone Creek to the Banff Jasper Highway. The Pipestone Creek divides this tongue of land from the remainder of this parcel. The parcel is relatively flat, level with the C.P.R. tracks at the south limit and about 6 feet above the Pipestone Creek. And a portion of the property consists of an island in the Creek which is low-lying and is about 2 to 3 feet above the Creek. The area in this parcel is approximately 51.89 acres. (This property is referred to and identified as A on Exhibit S-8 and also on the plan attached to Exhibit R-5.)

   The second parcel is essentially two pieces of land joined by an unopened road allowance in respect of which the Lake Louise Ski Lodge Limited held a licence of occupation. These two small pieces of land plus the area covered by the licence of occupation form a triangle of approximately 1.95 acres and the same is bounded by the confluence of the Bow River and Pipestone Creek and by the road to Lake Louise Station. (This parcel is referred to and identified as AA on Exhibit S-8 and on the plan attached to Exhibit R-5.)

An Agreed Statement as to Facts was executed by the parties to this action and it was filed as Exhibit S-1 at this trial.

In paragraph 3 of the said Agreed Statement as to Facts the subject lands are described by their metes and bounds descriptions as set out in their respective title documents registered in the Land Titles Office of the Province of Alberta. The title of all the subject properties, it is agreed, is subject to the terms and conditions of agreements referred to in Caveat 6160 FE (being a Notice of Agreement between C.P.R. and Lake Louise Ski Lodge Limited) and Caveat 2446 FJ.

By Order of this Court dated 3 March, A.D. 1967, *inter alia,* it was provided "That the issue to be tried is the value of the properties expropriated as of the dates of their expropriation."

And the said Order also further provided that:

The Suppliants will contend that as to the lands subject of Action No. 162332 were, at the time of expropriation, worth at least:—

(a) Lake Louise Ski Lodge parcels	$450,000.00
(b) Alfred Cooper parcel	15,500.00
(c) J. Stanley Boyle parcel	7,000.00
Total	$472,500.00

The Respondent denies such valuations.

The Respondent will contend that as to the lands subject of Action No. 162332 were, at the time of expropriation, worth not more than:—

(a) Lake Louise Ski Lodge parcels	$ 25,000.00
(b) Alfred Cooper parcel	5,800.00
(c) J. Stanley Boyle parcel	2,400.00
Total	$ 33,200.00

The Suppliants deny such valuations.

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The suppliants in evidence sought to establish the following values of their respective property as of the date of their expropriation, namely:

(a) J. Stanley Boyle ....$ 7,000
(b) Alfred Cooper ....$ 15,500
(c) Lake Louise Ski Lodge Limited
(i) as to the main parcel ....$ 87,000 or $270,000 or $280,000
(ii) as to the small parcel ....$ 6,000

The respondent in evidence sought to establish the values of the said properties expropriated as of their dates of expropriation as follows:

(a) J. Stanley Boyle .... $ 2,400
(b) Alfred Cooper ....$ 5,800
(c) Lake Louise Ski Lodge Limited
(i) main parcel ....$ 20,000
(ii) small parcel ....$ 5,000

It was common ground between the parties that (a) the subject properties lie in the area in the Banff National Park known as the Lower Lake Louise area; (b) that the area referred to as Upper Lake Louise area is about 2 miles west, north-west of Lower Lake Louise area; (c) that Lower Lake Louise area is about 36 miles north-west of the Town of Banff which is also in the Banff National Park; (d) that proceeding from Calgary north-west by highway the Town of Banff is first reached, being about approximately 74 miles and that proceeding further west and north-west Lower Lake Louise is about another 36 miles; (e) that (as admitted giving numbers, in paragraph 11 of the said Agreed Statement as to Facts, Exhibit S-1) the number of people visiting the Banff National Park was very substantial in the period 1955-56 being in the number of 701,199 people and that the numbers have been in substantial escalation since, and that such would occur was an inference that probably could have been made in 1956; (f) that the total expenditures for the administration and improvement of the Banff National Park area generally by the Department of Northern Affairs and National Resources each year from 1952 has been most substantial and has also been in escalation; and (g) that similar comments apply to the expenditures on the Trans-Canada highway running through the Banff National Park.

It was also common ground between the parties that there were very few sales of freehold property or transfers of leasehold properties of raw land in Lower Lake Louise to use as comparatives to assist the respective valuators of the parties to come to the conclusions they did as to the values of the expropriated properties at the date of expropriation in 1956.

At this trial, the whole of the evidence consisted of the said Agreed Statement as to Facts, certain questions and answers read in by the suppliants of the discovery of one Coleman, an officer of the respondent, certain deeds and other documents and plans and reports, all of which were admitted without further formal proof, and certain oral evidence, and a visit by the Court, (on motion of counsel and granted) of the Lower Lake Louise area, viewing the subject properties in particular, the highway to the Town of Banff and the Town of Banff.

The oral evidence of the suppliants was given by Mr. James Boyce, who with Alfred Cooper and J. Stanley Boyle owned all the shares in Lake Louise Ski Lodge Limited, Mrs. J. Stanley Boyle, widow and sole executrix and beneficiary of the estate of J. Stanley Boyle now deceased, and three witnesses who gave opinion evidence, namely, G. I. M. Young, a real estate appraiser of the firm of Stewart, Young and Mason, Toronto, Mr. G. E. Gordon of the firm of Underwood, McLellan and Associates Limited, Calgary, Consulting Professional Engineers and Land Surveyors, and Mr. Neville F. Bothwell of the same firm, Calgary, a Land Development Engineer.

The oral evidence of the respondent consisted of the evidence of Mr. Henry Bell-Irving, a real estate appraiser and real estate broker of Vancouver, B.C.

Before assessing the evidence as to value particularly, one general conclusion from the evidence may now be stated.

Counsel for the suppliants submitted that at the material time other purchasers could have purchased the subject lands and put them to the same use as the expropriating authority. Counsel for the respondent agrees there was in existence a market for the subject lands at that material time, but disagrees that the expropriating authority contemplated at the material time, or now is putting the lands to the same use that a possible purchaser or the former owners might have.

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In my opinion, considering the whole of the evidence adduced in this case, there was proof that there was a market for these subject properties but there was no proof given of any special adaptability or use of any of the subject properties. It follows therefore, that there is no special value to the suppliants within the meaning of the decided cases and as a consequence, market value in this case is the sole criterion of the values of the subject properties as of the date of expropriation. In this connection, the words of Rand J. in *Gagetown Lumber Co. Ltd. v. The Queen and Attorney-General for New Brunswick*[1] are apt:

> Market value, that is, the price at which a prudent and willing vendor and a similar purchaser would agree on, may be the sole determinant, exhausting compensation, but it may not be. Where the position of the owner *vis-à-vis* the land is not different from that of any purchaser, that value is the measure; where the owner is in special relations to the land, as in the case of an established business, the measure is the value to him as a prudent man, what he would pay, as the price of the land, rather than be dispossessed, that price thereafter, in effect, representing the capital cost of the business to which the profits would be related. But evidence of those relations issuing in special injury upon extrusion and their value in terms of money must be adduced. It is in this comprehensive view that in *Woods Mfg. Co. v. The King,* (1951), 2 D.L.R. 465, S.C.R. 504, 67 C.R.T.C. 87, by a unanimous judgment, the rule for compensation under the existing law was laid down definitively by this Court.

The evidence of the suppliants of market value of the subject properties as of the date of expropriation was put forward in this way.

Mr. G. I. M. Young, the real estate appraiser of the suppliant, made his evaluations in 1966 and employed two methods of evaluation in respect to the principal or main parcel formerly owned by the Lake Louise Ski Lodge Limited. (He employed only his first method, hereinafter referred to, in valuing the other subject properties.) This resulted, as above noted, in a range of value for the main parcel found by him of $87,000 using one method and $270,000 or $280,000 using the second method.

The first method he employed from which he made a valuation of $87,000 was one based upon other transactions of raw land alleged by him to be comparable to the subject property.

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[1] (1957) 6 D.L.R. (2d) 657 at 661-62.

The second method he employed from which he made a valuation of $270,000 or $280,000, resulted in an estimate of value based upon the potentialities of the subject property for development purposes which in turn was based upon a scheme of development prepared in 1966 by Underwood, McLellan and Associates Limited, and described in oral evidence by the said engineers Messrs. G. E. Gordon and Neville F. Bothwell.

In making his evaluation by the first method, namely, based upon comparable transactions of raw land, Mr. Young found difficulty finding many sales of freehold property or transfers of any leasehold property in the Lower Lake Louise area with which to compare the subject property. To make up for this deficiency, he used two properties just outside the town site of Banff, which is approximately 36 miles away from the subject property, *viz,* the lands on which there were built subsequently respectively, the Archway Motel, and the Bel-Plaza Motel (Items I and II respectively, Appendix "B", Exhibit S-93).

Mr. Young stated that this method would have been the sole one he would have employed in this case if there had been a greater number of transactions which he could have used as comparisons. But since there was this scarcity of alleged comparables, he advised counsel for the suppliants in 1966 to employ someone to prepare a possible scheme of development for the subject lands and for this purpose, Messrs. Gordon and Bothwell of the firm of Underwood, McLellan and Associates Limited were employed.

These latter gentlemen prepared a possible scheme of development for the subject lands in 1966 and gave evidence of it. Mr. Gordon's report was filed as Exhibit S-52 and also appears as Appendix "C" to the report of Mr. Young, Exhibit S-93.

Mr. Bothwell's report was filed as Exhibit S-62.

The elaborate plans of possible development for the subject lands made by Mr. Bothwell were also filed as exhibits. Exhibit S-63 is called Plan 1; Exhibit S-65 is called Plan 2; Exhibit S-64 is called Plan 3; Exhibit S-67 is called Plan 4; Exhibit S-66 is called Plan 5: and Exhibit S-68 is called Plan 6.

Basically, Plans 3 and 4 were plans of development of the subject lands without taking into consideration the

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crossing of the subject property by the Trans-Canada Highway in 1962 and Plans 5 and 6 were plans of development taking such into account.

These plans of development of Messrs. Gordon and Bothwell did not (a) take into account in any way the economic feasibility of the same and (b) did not establish that the probability of any person implementing such plans or some variation thereof, was a factor actually in the market in 1956.

Mr. Young, in employing these possible schemes of development of the subject property (i.e. of the main parcel formerly owned by Lake Louise Ski Lodge Limited) in doing his second method of evaluation also ignored entirely the economic feasibilities of the same. He also purported to compare theoretical sales of property in this scheme of development with actual sales of parcels of land in the town site of Banff, 36 miles away, which took place from 1955 to 1965. Mr. Young also accepted the figures of estimates of cost of construction of implementing of the said plans of Messrs. Gordon and Bothwell. He also said that the question of economic feasibility was one for the purchaser and not one with which he should be concerned.

Employing his second method, Mr. Young arrived at his said valuations of the subject property of Lake Louise Ski Lodge Limited main parcel, that is $280,000, based on Plans 3 and 4, and $270,000 based on said Plans 5 and 6, both as of the date of expropriation.

The suppliants, Lake Louise Ski Lodge Limited, in my view, from the evidence, clearly had none of such schemes in mind at the material time; and in addition, the evidence generally indicates that no one in the Lower Lake Louise area had either. Indeed, no evidence was adduced that any of such schemes would be economically feasible even to-day.

In my view, therefore, any evaluation of the subject property of Lake Louise Ski Lodge Limited main parcel, based on this second method of evaluation by Mr. Young, is of no assistance to the Court in determining what the market value of this property was at the date of expropriation. In fact, because there was no evidence adduced showing that the opinions of Messrs. Gordon and Bothwell and Mr. Young's opinion based on these two opinions were actually factors in the market in 1956, such evidence in

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respect thereto may be inadmissible *in toto*. (Compare Cattanach J. in *Molly James et al v. Canadian National Railway Company*[2]; *Raja Vyricherla Narayana Gajapatiraju v. The Revenue Divisional Officer, Vizagapatam*[3]; see also *Re Jupiter Estates Ltd. and Board of School Trustees, School District No. 61 of Greater Victoria*[4] per Davey J.A.; and *Pawson v. The City of Sudbury*[5] per Roach J.A.) In any event, if these opinions are admissible, they have such little weight that I am disregarding them in arriving at the findings I make in this action.

> The award states that it is based primarily upon the unanimous opinion that, if it had not been for the intervention of the expropriation, the land would have been legally subdivided into building lots at the date of the expropriation. From that it seems that the arbitrators concluded on the evidence, as they were entitled to do, that there were no legal or practical difficulties that might have prevented the subdivision of the 7 23 acres along the lines proposed. But the land had not been subdivided; it was still in acreage, and as acreage it ought to have been valued, but as acreage that was eminently suitable and ripe for immediate subdivision. However, that value could not be fixed by taking the aggregate of the selling value of the individual lots, and deducting future physical development costs, because that would merely give the highest amount that might eventually be realized from the sale of all the lots. No owner would pay to forestall expropriation of acreage the total amount he hoped to realize from an intended subdivision, because that sum would make no allowance for all the elements of cost and the business risks involved, such as actual cost of development exceeding the estimates; change in economic conditions that might depress prices, or slow, or prevent sales; interest on the cost of development, and on the capital invested in the project; the cost of selling; allowance for profit, without the prospect of which no owner would undertake the scheme; and the other substantial business risks inherent in any project requiring the investment of considerable sums of money.

For the purpose of completing the record, however, I am admitting the report of Mr. Young which contains not only his first said method of evaluation, but also his second method of evaluation. The registrar has numbered it Exhibit No. S-93.

In considering the suppliants' opinion evidence as to market value, therefore, I am taking into consideration only the evidence of Mr. Young in relation to his first method of evaluation based upon comparable sales of raw land.

[2] [1965] 1 Ex. C.R. 71 at 76.
[3] [1939] A.C. 302.
[4] (1966) 56 D.L.R. (2d) 414 at 419.
[5] [1953] O.R. 988.

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In this connection, as mentioned, it will be recalled that Mr. Young in valuing the main parcel of Lake Louise Ski Lodge Limited, used as alleged comparables not only the transactions he found in the Lower Lake Louise area, but also two transactions in the area just outside the Town of Banff, 36 miles away from the subject property, namely, the said motel properties upon which were built later respectively, the Archway Motel and the Bel-Plaza Motel.

In relation to the other subject properties, namely, (1) the other and such parcel formerly owned by Lake Louise Ski Lodge Limited, (2) the Cooper property, and (3) the Boyle property, Mr. Young employed his first method only in arriving at his valuation of the same as of the date of expropriation.

The respondent's witness as to value, Mr. H. Bell-Irving used two methods of evaluation, namely, firstly a value estimate made by market comparison and secondly (in relation only to the main parcel formerly owned by the Lake Louise Ski Lodge Limited) an estimate of land value based on the capitalization of projected net income from a theoretical development on the subject property of four successive twenty unit motel sites.

In employing his market comparison approach, Mr. Bell-Irving examined all the transactions in the Lower Lake Louise area and, like Mr. Young, found that there were relatively few freehold sales or leasehold transfers from which to make a comparison. He also examined freehold sales and leasehold transfers in the town site of Banff, 36 miles away, and in the area immediately adjoining the Banff town site. But he came to the conclusion that he must reject all these latter transactions in the Town of Banff site and adjoining it because, in his view, such properties were not comparable to the subject lands in Lower Lake Louise or indeed, to any property in Lower Lake Louise area.

In this latter respect, the data employed by Mr. Bell-Irving in his market comparison approach differ materially from Mr. Young's.

In one other respect the opinion of Mr. Young is based on data different than that used by Mr. Bell-Irving, namely, the fact that Mr. Young made no allowance for the C.P.R. covenants which the title to the subject properties were qualified referred to in Caveat numbered 6160 FE being Exhibit R-1, being a contract between the C.P.R. and Lake Louise Ski Lodge Limited.

Now before discussing the values respectively found through the market comparison approach by Mr. Young and Mr. Bell-Irving, three things are said.

First of all, I am of the opinion that it is not possible to compare sales of freehold and leasehold transfers in Lower Lake Louise area with such in the Town of Banff site or in the surrounding area, 36 miles away, for a number of reasons. Among such reasons are the fact that the Town of Banff has many more amenities which would cause the public to visit and live there in preference to Lower Lake Louise area. Such amenities for example, are a first class golf course, sulphur springs, an art school and all the usual shopping and eating facilities of a well-developed resort town.

Secondly, there is much flat land owned by the Crown in the Banff National Park between Eisenhower Junction, just north-west of the Town of Banff and the Lower Lake Louise area which is comparable to the Lower Lake Louise area, and which if demand warranted it, the Crown probably would lease in parcels to third parties for uses compatible with the Banff National Park regulations and policies.

The third thing that should be mentioned is that in approaching value, regard must be had to the existence of the covenants contained in the Agreement, Exhibit R-1, Caveat 6160 FE, registered at Calgary Land Titles Office on the 9th of July, 1943. (These are the same covenants which are contained in the documents Exhibits 34A and 34, see particularly Clauses 10 and 17). (Clause 17[6], *inter alia,* requires

[6] 17. The Company, to the intent that the burden of the following covenants may run with the land, and the Purchaser for himself, his executors, administrators, heirs, assigns and successors in title, respectfully covenant and agree with each other as follows:

(a) The Purchaser agrees that he will in the erection of the Lodge and tourist cabins herein provided for, comply with all regulations imposed by the Government of the Dominion of Canada in relation to the construction, erection or maintenance of buildings in the National Parks of the Dominion of Canada.

(b) Without in any way relieving the Purchaser from any liability under the Provisions of the immediately preceding paragraph hereof, the Purchaser will before erecting any building on the said property submit to the Superintendent of Sales, Department of Natural

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the purchaser of the subject lands to maintain a 25 foot set back of buildings and also to build not more than one lodge or hotel at any one time, such to contain not more than 20 rooms.)

As to these covenants, counsel for the suppliants addressed argument with supporting authorities that the same were null and void.

As to this, it may or may not be that in an action in which the validity of such covenants were put in issue, that such would be the decision of the Court. But because it is not in issue before this Court in this trial to decide whether these covenants are enforceable or not, including whether they are restrictive covenants or personal covenants, it is not necessary for me to make any adjudication in respect to such submission by counsel for the suppliants.

But in any event, as to the alleged invalidity of these covenants, there was no evidence put before this Court. Only the documents themselves were filed as exhibits. There was, however, evidence put in on the cross-examination of Mr. Bell-Irving as to the validity of such covenants. He was asked whether in making his evaluation he had asked for any legal opinion as to whether these covenants referred in this said Caveat were binding or not on a possible purchaser of the subject lands and on such lands,

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Resources of the Company at Calgary, Alberta, a sketch plan showing the type of construction of such building, and the manner in which the exterior of proposed buildings is to be finished, and will not commence the construction of such buildings until the approval in writing of the Superintendent of Sales has been obtained.

(c) Not more than one Lodge or hotel shall be built upon the said land at any one time, nor shall such lodge or hotel when built contain more than twenty rooms.

(d) The said lands, or any buildings to be erected thereon, shall not at any time be used for the purpose of a livery stable, blacksmith shop, lumber yard, hot dog or hamburger stand, or boarding house.

(e) That no building, nor its verandah, porch, bay windows or steps erected on the said lands shall be nearer than twenty-five feet from the front line of the said property.

(f) The Company for itself, its successors and assigns, covenants and agrees with the Purchaser that it will not for a period of ten years from the date hereof, permit any person, firm or corporation to erect, build or operate a Tourist Camp on those portions of Sections Twenty-seven (27) and Twenty-eight (28) in Township Twenty-six (26), Range Sixteen (16) West of the Fifth Meridian, not included in the lands herein sold.

to which he replied that he had contacted the Legal Department of the C.P.R. and they had told him that the covenants meant what they said.

Be that as it may, the validity of the covenants, as stated, is not something this Court has to decide in this action, and a prospective purchaser in 1956 would, in my view, take into consideration that there existed a notice of these restrictions as to the use of the subject lands and would give such fact the weight he considered appropriate.

Dealing specifically with the relative comparative sales used respectively by Mr. Young and Mr. Bell-Irving in arriving at their value based on such method, the following may be said:

First of all, in relation to the matter of the highest and best use of the property at page 2 of his report, Exhibit S-93, Mr. Young said (in reference to the main parcel formerly owned by the Lake Louise Ski Lodge Limited) "in the opinion of the appraiser the highest and best use of the subject property will be in accordance with the opinions expressed by Messrs. Underwood and McLellan in a suggested scheme of development".

As to parcels B and C shown on Exhibit S-8 and on the plan attached to Exhibit R-5, Mr. Young does not state any highest or best use, but from the evidence, I assume that he holds the same view as Mr. Bell-Irving, namely, that these parcels might have been purchased at the material time by some buyer to hold for speculation for some future development as yet undetermined.

Mr. Bell-Irving on the other hand in respect of Lake Louise Ski Lodge Limited main parcel (marked A on Exhibit S-8 and on the plan attached to Exhibit R-5) notwithstanding that he was not able to get any help from any person in the area, envisaged a development on it of a 20-unit motel in 1956 and similar developments of a 20-unit motel, in each of the years 1962, 1964 and 1966, as the highest and best use of this property. He did so on the basis that the Banff National Park authorities, in respect of their regulations, and the C.P.R., in respect to its restrictions in the said Caveat, would be reasonable and cooperate with a potential purchaser.

As to the small parcel formerly owned by Lake Louise Ski Lodge Limited (shown as AA on said Exhibit S-8 and on the plan attached to Exhibit R-5), Mr. Young gave no opinion as to its highest and best use in his report, but in his evidence said that it might have some commercial use.

Mr. Bell-Irving on the other hand was of the opinion that as of 1956 this parcel's highest and best use might be a development with an owner's house, public dining-room and eight motel units, which would be possible on the basis that there was available for building purposes part of the property held under licence of occupation, such part being between the two other parcels and which not having been acquired from the C.P.R., would escape the C.P.R. covenant referred to in the said Caveat 6160 FE restricting the numbers of units that could be built on it.

As stated, Mr. Young in making his estimate of value based on alleged comparable transactions of raw land just considered three such transactions. Two were just outside the Town of Banff, 36 miles away from the subject property. One was in Lower Lake Louise. The two parcels outside the Town of Banff are shown as Items I and II in Appendix "B" to his report, Exhibit S-93, (on which, as mentioned, respectively are now built the Archway Motel and the Bel-Plaza Motel) from which he purported to find the 1957 and 1954 cost respectively to the transferees of $3,896 per acre and $2,856 per acre.

The parcel in Lower Lake Louise is the one 1.62 acres of land located on the east side of the Banff Jasper Highway opposite what is referred to in the evidence as the Brisco land (the subject property in action B-314) north of the Post Hotel also referred to in the evidence. It sold in October 1952 for $3,500 or $2,160 per acre. This is listed as Item III in his report.

Originally this property had been sold in 1941 by the C.P.R. to James Boyce for $154 per acre. James Boyce sold this to one Lewis Sydney Crosby et al in 1952 for $2,160 per acre. The evidence is that Mr. Crosby sought to use this for a service station at the time of purchase.

This property of Crosby's was expropriated in 1956 and the title indicates that there was a settlement made by the Crown. The conveyance to the Crown recites the considerations as $5,000 but there were two transactions in connection with leases also entered into with the Crown about the same time regarding other property.

In my view, because this is a settlement of expropriation compensation and the details of it are not known, no weight can be given to this subsequent transaction in 1956 between the Crown and Crosby to assist the Court in finding the market values of the subject properties at the material times.

Not in his report, but in his evidence to support his opinion based on market comparison, Mr. Young did purport to use the transactions involving the Post Hotel commencing with the purchase from the C.P.R. of the whole of the land of which the land used for the hotel formed part, in 1941, and the sale of it in 1946, to assist him in arriving at the values he found employing his first method.

I am unable to draw any inferences from the Post Hotel transactions, however, because, among other things, the figures of allocation of costs of construction and acquisition of the various assets shown on the financial statement filed may or may not be valid as representing precisely the costs of the various items, and because I am unable to measure without evidence what sum should be allocated to goodwill. Therefore, for these two reasons, and for others it is not necessary to mention, it is impossible to make any finding of what the probable value of the Post Hotel land was, not only in 1946, but in reference to 1956 values.

Mr. Bell-Irving, in his market comparison approach, used one transaction only, namely, the said transaction concerning parcel D, plan 8189 FE being the sale of 1.62 acres from Boyce to Crosby in 1949 for $3,500 or $2,160 per acre. He makes the assumption that this sale was at arm's length and indicative of the market value per acre at that time. He admits that between the date of sale 1949 and 1956, there is no local evidence of any change in market value of raw land in the area. He points out that the total park east gate passenger entries increased between those dates by about eight per cent and notes that there is some percentage relation which may be coincidental with the increase in Town of Banff values based on the amounts paid by successful tenderers for leasehold lands in that area. He says that these figures do suggest that properties in Banff town site may have increased in value between 1952 and 1956 but queries whether Lower Lake Louise have increased to the same extent. He says he was unable to find evidence of a comparable demand in the Lower Lake Louise area. He, however, concludes as a rough crite-

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rion that the increase in Lower Lake Louise land values might be better than indicated by overall tourist intake figures. And, he concluded that he should make a round figure date adjustment of 25 per cent, which in his opinion is reasonable and might have been accepted by a buyer in 1956 in the absence of any evidence to the contrary.

From this he concludes that the 1956 price per acre of usable property in the large parcel formerly owned by Lake Louise Ski Lodge Limited, (parcel A, on Exhibit S-8 and on a plan to Exhibit R-5) should be $2,700 per acre.

Relating the usable property of this said parcel to the highest and best use, namely, for the development of four sites to establish on each 20-unit motels in each of the years 1956, 1962, 1964 and 1966, he takes four areas of seven acres each; and from this arrives at a price of a seven acre area of said parcel A in 1956 of $18,900.

In addition, however, to this raw land alleged comparative sale, Mr. Bell-Irving uses the sale nearby in the Lower Lake Louise area of a 7.64 acre property improved with a 22 unit motel on it, known as the Motel Lake Louise. It is located on the south-west side of Banff Jasper Highway and is close to the subject large parcel of Lake Louise Ski Lodge Limited. It sold in 1954 to one Gourlay for $75,000 for which sum he acquired the land, buildings and chattels. It was built on leasehold property. From this data (see page 33 of Exhibit R-5), he purports to find a 1954 indicated leasehold land value of $7,000. He then converts this $7,000 figure to a comparable figure for the freehold land of a seven acre parcel in the subject lands of Lake Louise Ski Lodge Limited in 1956 and purports to find an indicated 1956 freehold value of Motel Lake Louise land of $18,322 by making an economic analysis using projected earnings and, *inter alia,* making a $12\frac{1}{2}$ per cent addition to the figure found of freehold value as a possible adjustment for the change from 1954 to 1956.

Having thus come to the conclusion, using a market data approach that a seven acre freehold price in parcel A of the subject property of Lake Louise Ski Lodge Limited had an indicated value in 1956 of $18,900, and using an economic approach employing the Motel Lake Louise sale that this 7.64 acres of freehold land had an indicated 1956 value of $18,322, Mr. Bell-Irving then used his concept of the highest and best use of the main parcel of Lake Louise Ski Lodge Limited, (parcel A on Exhibit S-8 and on plan attached to Exhibit R-5) to find his 1956 market value of the whole parcel. (See page 36 of his report, Exhibit R-5.)

In so finding, he assumes that a person in 1956 would consider that each of the three other seven acre parcels of Lake Louise Ski Lodge Limited (envisaged in his concept of the highest and best use of the property) would sell for $18,900 in the years respectively 1962, 1964 and 1966. He then finds the present worth of all these sales, including the first sale, at $52,100. From this he deducts the estimated cost of bridging the Pipestone River to reach said parcel A, in the sum of $24,000 and of building a roadway, in the sum of $6,840. From this he gets an indicated value of $21,260 or in round figures $20,000 for this parcel.

Mr. Bell-Irving admits the economic approach is not usually the best one for evaluating any resort property, for many reasons. He also indicates and admits that there are many variables, such as projected rates of rental, occupancy rates, expenses, the capitalization rate, etc., and that changes in any of these will result in finding a different land value.

In considering his whole approach though, two matters are significant. Firstly, as mentioned, in considering his market data approach (see page 32 of Exhibit R-5), he estimated a 25 per cent increase in land values between 1949 and 1956 in arriving at a figure of $2,700 per acre, which he used for the purpose of developing his concept of the highest and best use of said parcel A (Exhibit S-8, and on the plan attached to Exhibit R-5), and to make his ultimate finding of 1956 market value.

Secondly, in using his economic approach, as also mentioned, he added $12\frac{1}{2}$ per cent as the indicated adjustment between 1954 and 1956 to obtain his indicated 1956 freehold value of the Motel Lake Louise land of $18,322.

So much for a discussion of the evidence.

Speaking generally in coming to a conclusion, I consider that only transactions in the Lower Lake Louise area should be considered as comparable in any material and substantial way so as to reach a correct finding of market value in this case, (as I have indicated earlier in these Reasons).

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Of substantial importance also in this case, because, *inter alia*, of the lack of any number of comparable market sales, is the history of the subject properties in this particular case.

The history of the sales and development of the subject properties in brief is as follows:

The whole of the subject property, namely, parcel A and parcel AA of the Lake Louise Ski Lodge Limited and parcels B and C owned by Boyle and Cooper respectively, plus the property that constitutes the Post Hotel which was subsequently sold to a third party, plus another strip opposite the Post Hotel sold to one Brisco, (which is the subject of another action numbered B-314) (all of which parcels are so shown and referred to on Exhibit S-8 and on the plan attached to Exhibit R-5) were all purchased from the C.P.R. in 1941 for $6,000, and were subject to the Caveats contained in said instrument numbered 6160 FE and 2446 FJ.

The first transaction after the CPR purchase that took place was in respect to a small parcel of it which was transferred to James Boyle, on which subsequently in 1949 was built a service station and a store, both of which are still owned by the Boyle estate.

Then parcel B was given to James Boyle without any consideration.

Then parcel C is deeded to Mr. Cooper without any consideration.

Then in late 1941 or in 1942 the Post Hotel was built on a two acre parcel. This hotel remained vacant during the war years and was sold in 1946 by the Lake Louise Ski Lodge Limited.

Then in 1947 Lake Louise Ski Lodge Limited authorized Mr. Cooper, who at the time was making frequent trips to Calgary, to sell the better lots (on a rough plan of parcel A) for $300 each, but nothing came of this because there was no market for the sale of any of these proposed lots.

Then in 1953, the shareholders of Lake Louise Ski Lodge Limited made a draft division among themselves of said parcel A (see Exhibit R-3). This proposed division would have given Boyle, Cooper and Boyce, each a ten acre parcel and also a smaller 2.75 acre parcel. This draft plan for division was submitted to the Banff National Park authorities, but they refused permission to divide this land, and so nothing came of it.

In short, Lake Louise Ski Lodge Limited built the Post Hotel, which was subsequently sold, on a two acre parcel of the total they had received from the C.P.R., and gave away all the rest of this land which fronted on a highway. What remained at the date of expropriation in 1956, was the poorest part of this land. It did not front on any highway. To reach it, a bridge would have to be constructed over the Pipestone River which in 1956 would have cost at least $24,000 (for a wooden bridge), and a road would have to be constructed which would have cost at least $6,000. And as late as 1953, the shareholders of the Lake Louise Ski Lodge Limited apparently thought there was no immediate market for parcel A, and attempted to divide it into three titles, each to take part of it, obviously to hold same for some indefinite purpose some time in the future, but permission to so divide was refused. In addition, no survey was made of the subject property, no engineering study and no economic feasibility investigation was made by the suppliants at any time.

This was the situation that existed in 1956. The only hope giving some new potential to the property was the building of the Trans-Canada Highway, (then expected in 1960) in consequence of which then was an expected substantial increase in the number of people who by motor car would visit the Banff National Park area and therefore Lower Lake Louise area would receive some share of this traffic and whatever economic benefit that would accrue attributable to it.

In addition, the owners of the subject properties, at all material times, all knew that they had to comply with the Banff National Park regulations. They knew that their properties were subject to such limitations. They also knew, as it was admitted in evidence by Mr. Boyce and Mrs. Boyle, that they had to comply with C.P.R. covenants. That was their belief. The situation was also, and still is, that Lower Lake Louise area is not a year-round resort area. Tourists come in the summer months, skiers come in the winter, but of the skiers, a large majority are day skiers from Calgary.

Undoubtedly also, in 1956 a potential buyer of the subject lands would know that there was little freehold in the whole Banff National Park. He would know of the limitations as to the use that could be made of the properties

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imposed by the National Park regulations and policies and by the C.P.R. covenants. He might consider that the freehold had certain monopolistic value because there was so little of it, but he would realize also that it would be subject to the devaluing influence caused by the situation that most of the existing private enterprises are on leaseholds with good tenure at very low ground rentals and that as demand for facilities increased, the National Park authorities would probably make available on leases, other areas of low-lying land, especially between the Banff town site and Lower Lake Louise, for purposes which would be compatible with providing the amenities for tourists as citizens of Canada and in competition with anything that could be provided in the Lower Lake Louise area. This latter is a proper inference from part of the evidence of the discovery of Mr. J. R. B. Coleman, Director of Banff National Park of the Department of Northern Affairs and National Resources of Canada, read in and made part of the suppliants' case, *viz*:

404 Q. Let us put it this way: When was the department aware of the firm survey that a highway would be built through the Lake Louise area, what year?
A. I would have to inform myself on that.

405 Q. Was it before 1956?
A. Yes.

406 Q. That is all you know. And highways, that knowledge coming into the department and to men of your calibre and experience, it would leave you with the opinion, I am certain—and I ask you if that is correct—that there would be more people coming into that area?
A. Yes, it could be correct that there would be more people coming once the Trans-Canada Highway had been completed.

407 Q. Because the majority of people that do come to Banff—and I read out the number from 1955 to 1965, and whether they are exact or not doesn't matter, but they are there—come by automobile rather than any other source?
A. Yes

408 Q. Right. And if they are going to come there, services must be given to those people; that has been the policy of the parks for a number of years?
A. As demand increased we would endeavour to increase our facilities.

409 Q. And the demand has increased since 1945 steadily, there has been steady growth?
A. Not noticeably immediately after 1945.

410 Q. All right. Would you say from 1950?
A. I would say rather from the mid-50's.

411 Q. The mid-50's, and then the demand became fairly great?
A. Yes.

In relation to the opinion evidence adduced, I am of the view that the opinion of Mr. Bell-Irving should be preferred to that of Mr. Young; and that the opinion of Mr. Bell-Irving in the main, represents the correct approach to market value in this case. Among the reasons why I come to this conclusion is, that Mr. Bell-Irving gave a realistic opinion as to the highest and best use of each of the respective subject properties, whereas Mr. Young did not; Mr. Bell-Irving used as comparables in his market data approach land in Lower Lake Louise area only, whereas Mr. Young based a substantial part of his evidence in relation to parcel A on the grandiose schemes of development of Messrs. Gordon and Bothwell which I do not think are of any help and sales in the Town of Banff and just outside; that in relation to parcel A, Mr. Bell-Irving highlights as the main debility of the property, the necessity of building a bridge and roadway, and in relation to parcels B and C, the question of whether or not access from the Trans-Canada Highway could be obtained by a purchaser of these parcels.

One other reason that Mr. Young's evidence is not to be preferred, is because I do not think Mr. Young, in preparing his report, (which was filed as Exhibit S-93) has done anything more than counsel could have done themselves.

In summary, therefore, the views of the owners of the subject properties at the material times and the whole history of the property of which the subject properties are parts, are most vital. The views also of all persons in the area at the material time of the expropriation are also most relevant. These views and history, considered in relation to and in conjunction with the only sale of raw land, the Crosby sale, and the only transaction from which an economic approach can be employed as a check against the market data approach, namely, the Motel Lake Louise transaction, and the hope for financial return arising from the substantial increase in traffic to the area expected as a consequence of the completion of the Trans-Canada Highway, the problem of access to parcel A (by bridge and road only) and the problem of access to parcels B and C to Trans-Canada Highway are the main evidentary basis for the determination of market value of the subject properties as of the date of expropriation made in this case.

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The said market values of the subject properties, I find as follows:

(a) Lake Louise Ski Lodge Limited

(i) main parcel (parcel A on Exhibit S-8 and on plan attached to Exhibit R-5).

I accept the 1956 market value of seven acres found by Mr. Bell-Irving by employing his two methods, that is $18,900 or $18,322 and am of the view that a potential buyer would in his mind round such figures to $20,000. I also accept his concept of the highest and best use of this parcel, namely, four seven acre successive developments of 20-unit motels in a time schedule of approximately 1956 to 1966; and that the balance of the property would have little monetary value to the owner and therefore should not be considered in determining the market price of the whole parcel. I also accept the figure of bridging and road costs of $24,000 and $6,840 respectively.

A buyer therefore, would probably use the figure of $1,000 per motel site to make his judgment as to what he would pay for parcel A.

But I do not think a buyer in 1956 would discount the future site costs (see sites B, C and D, page 43, Exhibit R-5) in the way suggested by Mr. Bell-Irving. I am of the opinion that a buyer in 1956, if he would be prepared to buy at all, would be of opinion that values would go up in the years after 1956 and this would take care of all the unknown costs, including interest on his investment, while waiting for demand to arise so that he could economically complete this scheme of development. In other words, he would think of $1,000 per motel site as the cost to him in 1956.

This leads to the conclusion, therefore, in my view, on the evidence, that the market price in 1956 of this parcel was $50,000 (rounding the figure of $49,160), computed as follows:

Four sites at $20,000 each		$80,000
Less cost of Bridging the Pipestone River	$ 24,000	
Less cost of 1,200 feet of road at $5.70	$ 6,840	30,840
		$49,160

(ii) smaller parcel (parcel AA on Exhibit S-8 and on plan attached to Exhibit R-5).

I adopt the opinion of Mr. Bell-Irving as to the highest and best use of this property and his value of this land per acre and conclude that its market value as of the date of the 1956 expropriation was $5,300.

(b) J. Stanley Boyle and Alfred Cooper properties (that is parcels B and C—Exhibit S-8 and on plan attached to Exhibit R-5).

These properties have highway frontage of 600 and 650 feet respectively and consist of 2 acres and 4.40 acres respectively. The problem of access to the Trans-Canada Highway would be paramount in the mind of a speculator buyer, in my view in 1956, and he would not buy at all unless he did think he had some hope of getting some type of access. I think such a buyer would only buy if he could acquire both of these properties and in view of the evidence of the history of the association of Boyle and Cooper, this would seem to be a probability. I think such a buyer in 1965 would discount any indicated market value of property very heavily and I am of the opinion that such discount would be 50 per cent.

I accept the indicated 1956 market value of raw land in the area given by Mr. Bell-Irving of $2,400 per acre and find therefore, the 1956 market value at the date of expropriation of parcel B was $2,400 and parcel C was $5,280.

I also allow simple interest on the said sums at 5 per cent from the 29th day of August 1956, notwithstanding the unconscionable delay in bringing these claims for compensation to trial. I am, however, unable to assess which of the parties was to blame, or more to blame, for this delay and so, I am giving the benefit of this doubt to the suppliants.

As to costs, I think the suppliants are entitled to them with some abatement. There were two elaborate models prepared of the subject properties which were filed as Exhibits S-58 and S-59. The construction cost of them obviously was substantial. But they were of no use whatsoever

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in this adjudication. Accordingly, I do not allow any item of costs for the construction and preparation of these models.

In addition, Messrs. Gordon and Bothwell, who prepared these grandiose possible schemes of development of the main parcel of the subject property of Lake Louise Ski Lodge Limited, did not assist the Court in any way except to confirm that such schemes are of no assistance in adjudicating the compensation payable for raw land when such schemes of development were not factors in the market at the date of expropriation. In my opinion, I see no reason why they were required to go to all this trouble or were called as witnesses because the jurisprudence in respect to such evidence in relation to the problem of the said properties is quite clear. I therefore do not allow any costs for these witnesses or the cost of producing any of these plans.

Ottawa 1967

22 juin

18 août

ENTRE:

HERVÉ HOULE .... DEMANDEUR;

ET

MONCTON PUBLISHING COMPANY LIMITED .... DÉFENDERESSE.

Brevet d'invention—Loi sur les brevets, S.R.C. 1952, c. 203, article 28(1)(c)—Invention mise en usage public et en vente plus de deux ans avant dépôt de demande de brevet, contrairement à la Loi—Action pour infraction à un brevet d'invention—Objet de l'invention—Cartes de bons ou jetons utilisés pour faciliter le commerce du lait—Action déboutée avec dépens.

Le demandeur a poursuivi en justice la défenderesse pour infraction à son brevet d'invention, dont cette dernière a fait le dépôt de sa demande de brevet le 8 mai 1957. L'invention du demandeur avait pour objet des cartes de bons ou jetons en carton, de forme circulaire, utilisés pour faciliter le commerce du lait. Ces jetons consistaient en une «bande» de dix billets qui étaient échangés pour une certaine quantité de lait. Ces bons s'inséraient dans la partie supérieure d'une bouteille de lait et que l'on pouvait enlever en plaçant le doigt dans un trou concentrique situé au centre du jeton.

D'après la déclaration du demandeur, dans son examen «on discovery» tenu le 21 septembre 1966, il a commencé à fabriquer, produire et vendre ces bons ou jetons dès l'année 1949 et a ainsi continué à les utiliser jusqu'en 1955 sans toutefois en faire la demande de brevet de dépôt dans les deux ans de la date où il avait obtenu son brevet d'invention.

Jugé: En vertu de la loi, un inventeur peut obtenir un brevet à condition qu'il en fasse la demande dans les deux ans de la date où il en fait un usage public ou une vente publique au Canada. Sans cette restriction, un inventeur pourrait placer une invention sur le marché pendant des années et ne demander un brevet d'invention que lorsque quelqu'un d'autre décide de copier son invention. Il obtiendrait ainsi une période de monopole dépassant les dix-sept années prévues par le statut.

2. Dans cette cause, il appert que le demandeur a mis son invention en usage public et en vente au Canada plus de deux ans avant le dépôt de sa demande de brevet au Canada contrairement à l'article 28(1)(*c*) de la *Loi sur les brevets*.

3. Conséquemment, l'action du demandeur est déboutée avec dépens.

ACTION pour infraction à un brevet d'invention.

Kalman Samuels pour le demandeur.

E. Foster et *H. Senécal* pour la défenderesse.

NOËL J.:—Il s'agit d'une action pour infraction au brevet d'invention du demandeur (portant le numéro 545,592 et dont le dépôt de sa demande fut fait le 8 mai 1957) par la défenderesse, une corporation créée en vertu des lois du Nouveau-Brunswick, et ayant son bureau-chef à 18, rue Potsford, Moncton, Nouveau-Brunswick. L'invention du demandeur a pour objet des cartes de bons ou jetons utilisés pour faciliter le commerce et se réfère spécialement à des séries de billets circulaires découpés sur un carton. Ces bons ou jetons sont surtout utilisés pour faciliter le commerce du lait, le client se procurant périodiquement une bande de billets (comprenant dix billets, si l'on se réfère au dessin du brevet d'invention du demandeur) qu'il échange pour une certaine quantité de lait.

Dans son brevet le demandeur admet que le brevet d'invention canadien Tremblay et al, portant le numéro 464,734, ainsi que celui de Miller, portant le numéro 359,668, et par conséquent antérieurs au sien, ont pour objet des billets circulaires qui s'insèrent solidement dans la partie supérieure d'une bouteille de lait et que l'on peut enlever en plaçant le doigt dans un trou concentrique situé au centre du bon.

Il prétend, cependant, dans son brevet que par suite de certains défauts de construction, ces bons n'ont jamais été grandement utilisés. Quant à l'invention de Tremblay, dit-il, les bons ou jetons doivent être détachés en suivant une

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ligne pointillée ou une série de perforations espacées. Ce genre de perforations dans du carton d'une certaine épaisseur produit une «ligne de rabattement facile», mais il est quand même difficile de détacher le carton à cet endroit à moins qu'il ne soit plié à plusieurs reprises. Le détachement des bons ou jetons du carton se fait difficilement, si l'on veut s'assurer que les bons ou jetons ne soient mutilés. Les mêmes commentaires s'appliquent à l'invention Miller avec la différence ici qu'il n'est pas possible de rabattre le carton avant de détacher les bons ou jetons comme dans le cas de l'invention de Tremblay parce que la ligne de pliage est une courbe et, par conséquent, le danger ici d'endommager les bons ou jetons est accru.

De plus les livreurs de lait ont l'habitude de garder un nombre de cartons dans leurs poches en plus de ceux qu'ils gardent dans leur véhicule de livraison. Les cartons-bons construits suivant les brevets de Tremblay ou Miller ont, d'après le brevet du demandeur, une tendance à plier à des endroits où ils ne devraient pas l'être. Il est, par conséquent, nécessaire, en pliant ces bandes de carton, de prendre bien soin de ne les plier que sur les lignes perforées.

Le but déclaré de l'invention du demandeur Houle est de produire un carton de bons ou jetons de lait du même genre que ceux déjà mentionnés, dont les bons ou jetons puissent être facilement détachés avec peu de risque de mutilation et qui puissent aussi être pliés et ainsi facilement placés dans une poche d'habit.

Examiné par le procureur de la défenderesse le 21 septembre 1966, le demandeur déclara, aux pages 28, 29, 30, 37, 38, 40, 43 et 44 de l'interrogatoire «on discovery» que dès l'année 1949, il avait commencé à produire les bons ou jetons de lait de forme circulaire avec un trou à l'intérieur «plus ou moins dans la forme pour laquelle» il avait obtenu un brevet, «à peu près identiques à ceux pour lequel» il avait obtenu un brevet (p. 29) qu'il a utilisé lui-même et qu'il a d'ailleurs vendu. Il déclare qu'il en a produit et vendu en 1950, 1951 et par la suite (p. 30) en 1953, 1954, 1955, tel qu'il appert d'ailleurs des relevés de comptes se rattachant à son exploitation. A la page 37 il réitère que les bons qu'il produisait au cours des années 1950 à 1955 étaient identiques à ceux qui sont décrits au dessin annexé à la description de son brevet d'invention portant le numéro 545,592, ajoutant:

> J'ai jamais changé de forme, bien, excepté il y a quelques améliorations qui ont été faites pour les lignes ici, les coupures, car c'était pour . . . Dans une invention, c'est comme le téléphone, avec les années, on fait des améliorations.

et à la page suivante, 38, il précisa davantage sa pensée, en réponse à une question du procureur de la défenderesse, à savoir s'il produisait depuis 1950 des bons de billets en forme presque identique au dessin de son brevet, comme suit:

> Oui, oui, excepté quelques améliorations qu'il y a eu de même; il y en a quelques-uns qu'on a été obligé de faire une petite ouverture pour que les clients accrochent leur carte de bons dans les armoires—ça, des fois, des clients demandaient un surplus, on ne refusait pas de le faire mais seulement l'ensemble . . .

A la page 40, il répète qu'il a produit des billets à peu près identiques à ceux décrits au dessin pièce D-4 (soit le dessin de son brevet) mais qu'après 1950 il avait probablement ajouté une amélioration, soit des lignes pointillées. Il ajouta cependant à la page 41 que certains clients demandèrent et obtinrent dès le début de sa production de mettre des pointillages de sorte que certains des billets qu'il avait produits au cours des années 1950 et 1952 étaient identiques au dessin de son brevet (cf. p. 42).

Enfin, aux pages 43 et 44, on lui repose la question une dernière fois et il répond affirmativement qu'au cours des années 1950 à 1955 il avait produit et vendu des cartes de bons de lait de forme circulaire identiques au dessin qui apparaît à la pièce D-4. De plus, il appert aussi de sa réponse qu'il aurait agi ainsi parce qu'il avait demandé un brevet pour les bons ou billets circulaires avec trou concentrique (brevet qu'il n'a d'ailleurs pu obtenir) et qu'il se croyait protégé par cette demande. Il n'a par la suite réussi à obtenir qu'un brevet d'amélioration, soit celui qui fait l'objet du présent litige.

C'est sur la foi de ces déclarations répétées que le Président de cette cour, soucieux de réduire autant que faire se peut, les frais qu'un procès long et coûteux pourrait entraîner pour le demandeur, décida, le 7 juin 1967, de fixer au 22 juin 1967, à Montréal, l'audition de cette cause la restreignant, cependant, à la seule question de savoir si ces

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bons ou jetons de lait tels que décrits et réclamés dans le brevet d'invention du demandeur, ont été vendus au Canada par le demandeur, l'inventeur mentionné audit brevet, plus de deux ans avant le dépôt de sa demande de brevet au Canada suivant le sous-paragraphe (*c*) du paragraphe (1) de l'article 28 de la *Loi sur les brevets* qui se lit comme suit:

> 28. (1) Sous réserve des dispositions subséquentes du présent article, l'auteur de toute invention ou le représentant légal de l'auteur d'une invention qui
>
> (*a*) n'était pas connue ou utilisée par une autre personne avant que lui-même l'ait faite,
>
> (*b*) n'était pas décrite dans quelque brevet ou dans quelque publication imprimée au Canada ou dans tout autre pays plus de deux ans avant la présentation de la pétition ci-après mentionnée, et
>
> (*c*) *n'était pas en usage public ou en vente au Canada plus de deux ans avant le dépôt de sa demande au Canada,*

Suivant cet article, un inventeur peut obtenir un brevet à condition qu'il en fasse la demande dans les deux ans de la date où il en a fait un usage public ou une vente publique au Canada. Sans cette restriction, un inventeur pourrait placer une invention sur le marché pendant des années et ne demander un brevet d'invention que lorsque quelqu'un d'autre décide de copier son invention. Il obtiendrait ainsi une période de monopole dépassant les 17 années prévues par le statut. Il est par conséquent dans l'intérêt public qu'un inventeur fasse sa demande dans la période de deux ans de l'usage public ou de la mise en vente de l'invention sans quoi il perdra son droit d'obtenir un brevet pour cette invention.

C'est à cause des réponses données aux questions précises posées par le procureur de la défenderesse à l'interrogatoire «on discovery» du demandeur, à l'effet qu'il avait fabriqué et vendu une quantité de bons circulaires identiques en tout point à ceux apparaissant sur le dessin annexé à son brevet d'invention que les procureurs de la défenderesse, conformément à la règle 155c de cette cour, présentèrent une motion demandant à la cour des directives quant à la marche de cette instance. Le demandeur, lors de la présentation de cette motion, fit valoir au Président, par l'entremise de son procureur, qu'il pourrait, s'il en avait l'occasion, expliquer les réponses qu'il avait ainsi données et clarifier le témoignage qu'il avait rendu.

C'est dans ces circonstances que la présente cause fut amorcée et que le demandeur fut entendu comme témoin de la part du demandeur et qu'un M. Hicks fut entendu de la part de la défenderesse. M. Hicks qui est à l'emploi d'un producteur et distributeur de lait déclare qu'il rencontra le demandeur en 1950 à Montréal et discuta avec lui de la possibilité d'obtenir une quantité de ces bons ou jetons pour sa compagnie, la laiterie Sunrise, et le demandeur y consentit. Ces billets, d'après Hicks, ainsi vendus à sa compagnie de 1950 à 1960, étaient en tout point semblables au carton de dix billets apparaissant au dessin du brevet d'invention du demandeur.

Le demandeur Houle, d'autre part, confirme qu'il avait vendu des billets à M. Hicks avant l'année 1957 mais déclare qu'à ce moment, le poinçonnage de ses cartes était fait avec une «roule» soit une lame circulaire faite comme une lame de rasoir et qu'après 1957, il se servait de matrices et d'un morceau d'acier d'une épaisseur d'un demi-pouce, rond et avec un trou dans le centre. D'après Houle, la seule différence entre les bons ou jetons de lait antérieurs à 1957 et subséquents à cette date, c'est que ceux fabriqués par la «roule» ne donnaient pas une perforation aussi bonne que ceux fabriqués par les matrices.

Le demandeur ne réussit pas, par son témoignage à l'enquête, à établir que les réponses claires qu'il avait données à son interrogatoire «on discovery» lorsqu'il identifia le dessin annexé à son brevet d'invention et admit qu'il avait vendu des billets, jetons ou bons en tout point identiques à ceux qui apparaissent sur le dessin de son brevet, doivent être corrigées. Au contraire, il fut établi que les billets, jetons ou bons qu'il a vendus avant 1957 et par la suite, étaient en tout point identiques à ceux qui apparaissent au dessin de son brevet. Les meilleurs résultats obtenus par le moyen des matrices ne changent en rien, en effet, l'invention du demandeur si l'on s'en tient au champ couvert par son brevet.

Qu'il en ait vendu, d'ailleurs, est aussi confirmé, comme nous l'avons déjà mentionné, par le témoignage de M. Hicks, le représentant de la laiterie Sunrise, l'un des clients du demandeur et par les relevés de comptes du demandeur qui témoignent aussi de la quantité vendue.

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Que le système de «roule» n'ait pas donné une perforation aussi bonne ou satisfaisante que le système de «matrice» ne change en rien l'invention du demandeur, ni n'a-t-il permis d'autre part un meilleur pliage du carton de billets pour le placer dans la poche du livreur. Peu importe en effet que le demandeur ait donné au public, ou mis sur le marché, ou vendu ses cartons de billets fabriqués par le moyen de la «roule» ou de la «matrice», il me faut quand même décider et c'est d'ailleurs la conclusion à laquelle j'arrive, qu'il a donné son invention au public ou, pour utiliser le langage du statut, l'a mis «en usage public ou en vente au Canada plus de deux ans avant le dépôt de sa demande au Canada», contrairement à l'article 28(1)(*c*) de la *Loi sur les brevets*.

Montréal 1968

2 fév.

Ottawa 22 mars

ENTRE:

CHARLES-ÉDOUARD ST-GERMAIN ......APPELANT;

ET

LE MINISTRE DU REVENU NATIONAL ....INTIMÉ.

Impôt sur le revenu—Loi de l'Impôt sur le revenu, S R.C. 1952, c. 148, articles 3, 4, 8(1)(b)(c), 137(2)(a)—Code Civil de Québec, articles 424, 425, 1640—Additions et améliorations faites à la propriété détenue par l'actionnaire, payées par la compagnie locataire, constituent un bénéfice et des avantages pour l'actionnaire—Appel débouté.

Le ministre a cotisé le contribuable précité en ajoutant une majoration de $71,668.43 à ses revenus imposables, soit, pour les années fiscales 1959 ($2,596), 1960 ($20,963) et 1961 ($48,108). Selon l'avis du ministre, ces impositions résultent de certains bénéfices pécuniaires réalisés par le contribuable, en sa qualité d'actionnaire unique de Superior Window Company. Les dispositions des articles 8(1) et 137(2) de la *Loi dė l'Impôt* sont applicables en l'occurrence.

St-Germain interjeta vainement appel de cette majoration devant la Commission d'Appel de l'Impôt. De cette décision, il entend se pourvoir devant cette Cour.

L'appelant a été, jusqu'à 1962, le propriétaire détenteur de la totalité des 313 actions du capital-actions de la compagnie Superior Window Company Ltd. Il défrayait toutes les impenses de la compagnie et, en retour, en retirait seul tous les avantages et bénéfices.

Au cours des années d'imposition dont il s'agit, le contribuable a loué à sa compagnie, à raison d'un loyer annuel de $6,600, le terrain et la bâtisse ci-dessus érigée pour l'exercice de son entreprise.

Jugé: L'appelant, n'ayant jamais renoncé à son droit d'accession (*c.f.* 415CC) devenait seul et unique propriétaire des additions et améliorations faites à sa bâtisse puisque, en même temps, il assumait les fonctions de locateur et de locataire. L'article 1640 du *Code Civil* n'a pas son application ici.

2. Que la plus-value ainsi assurée aux immeubles de l'appelant, à même les revenus de sa compagnie, lui a procuré un bénéfice et des avantages en sa qualité d'actionnaire unique, «*qua* shareholder», en vertu des dispositions des articles 8(1)(*c*) et 137(2) de la *Loi de l'impôt.*

3. L'appel est débouté avec dépens.

APPEL d'une décision de la Commission de l'Impôt.

Maurice A. Régnier et *Peter F. Cumyn* pour l'appelant.

Alban Garon et *J. C. Sarrazin* pour l'intimé.

DUMOULIN J.:—Le contribuable précité interjette appel d'une décision de la Commission d'Appel de l'Impôt, en date du 19 mai 1967, concernant les années fiscales 1959, 1961 et 1962.

La Commission de l'Impôt maintenait les cotisations arrêtées par le ministère du Revenu national qui ajoutaient les montants ci-dessous aux revenus imposables de l'appelant, soit, pour l'exercice 1959, $2,596.55, pour 1960, $20,963.28 et, finalement, pour 1961, $48,108.60; au total une majoration de $71,668.43.

Selon que relaté dans une pièce au dossier, les parties s'entendent sur les faits suivants:

1. L'appelant était, jusqu'en 1962, le principal actionnaire de la compagnie «Superior Window Co. Ltd.», ci-après désignée «la compagnie y détenant la grande majorité des parts»;

2. Ladite compagnie occupait, pour les fins de son commerce, de 1959 à 1962, un terrain et une bâtisse qui appartenaient à l'appelant;

3. L'appelant était propriétaire de ces terrain et bâtisse depuis environ 1953, et en avait acquis la propriété à un coût d'environ $45,537 56;

4. Cette location, par la compagnie précitée, existait en vertu d'un bail verbal passé entre l'appelant et ladite compagnie;

5. De 1959 à 1961, inclusivement, la compagnie effectua des améliorations et additions d'une grande valeur sur lesdits terrain et bâtisse, dont la construction d'un entrepôt d'allonges tant sur l'entrepôt que sur la bâtisse originaire.

Aux précédentes admissions, il convient d'ajouter quelques précisions apportées par Charles-Édouard St-Germain qui témoigna assez longuement à l'audition de la cause.

La compagnie Superior Window Company Ltd., dont l'entreprise en était une de fabrication de fenêtres isolantes, fut constituée dès 1953, en vertu de la *Loi des compagnies de Québec.* De 1953 à 1958, Édouard St-Germain était

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propriétaire de la totalité des 313 actions du capital-actions de la firme, dont il était aussi, il va sans dire, le président et maître absolu.

En 1958 ou 1959, continue le témoin, Jean-Paul Gélinas, alors gérant général de la compagnie, aurait acquis 92 de ces 313 actions à raison de $250.00 l'unité, en cédant 50, peu après, à un autre employé, Jean-Paul Poirier, gérant des ventes.

Que ces transactions aient été réelles ou empreintes d'opportunisme, cela n'importe guère dans le contexte de ce litige, compte tenu de ce que durant ce bref intervalle, St-Germain ne possédait pas moins de 65% des actions de sa compagnie et de sa déclaration, qu'en février 1962, il redevenait propriétaire des 313 unités du capital-actions, 6 mois avant le 9 août, même année. A cette date, St-Germain vendait en bloc ses actions à la Maison Bienvenu Limitée de Montréal (voir la pièce A-2, p. 22 au cahier déposé de la preuve littérale). Concurremment, Superior Glass Window Company Ltd., alias Charles-Édouard St-Germain, pour satisfaire aux dispositions procédurières de la Loi, transportait à un simple prête-nom, l'emplacement formant partie du lot 1106 des plan et livre de renvoi officiels de la paroisse Notre-Dame de St-Hyacinthe... «avec bâtisses dessus érigées portant les numéros civiques 4475 et 4477 dudit Boulevard Sir Wilfrid Laurier et toutes dépendances y attachées»; pièce A-3, page 25 (le souligné est ajouté). Quant au prix de vente, il s'élevait au chiffre de $275,000.00, les affaires de la vitrerie attestant, depuis le début, une progression constante.

St-Germain, propriétaire de l'immeuble, avait consenti à Superior Window Company, dès 1953, un bail verbal à raison d'un loyer mensuel de $435.00 haussé à $550.00 en 1958 ou 1959. A l'étage supérieur de la manufacture, deux logements étaient loués à des particuliers.

Un second et dernier témoin, Pierre Lacaille, âgé de 37 ans, comptable agréé de son état, revisait la comptabilité de la compagnie. Il nous rapporte le fait révélateur et significatif qu'en 1959 et 1960, le coût du chauffage de la vitrerie, celui des assurances et toutes les taxes civiques et scolaires afférentes à Superior Glass Window Company furent acquittés par Charles-Édouard St-Germain personnellement. En 1961, cependant, selon le conseil professionnel du comptable Lacaille, St-Germain se ravisa quelque peu et ne solda de ses deniers que l'intérêt semestriel des deux hypothèques consenties lors de l'achat de la bâtisse en 1953.

De tout ceci, il ressort irréfutablement que la compagnie dont il s'agit était la chose propre, l'entière propriété de l'appelant qui en défrayait les charges civiques ou autres et, conséquemment, en percevait tous les avantages et bénéfices.

Abordons maintenant le point litigieux du débat: l'interprétation statutaire qu'il convient d'appliquer à ces impenses de $71,668.43, réparties sur la période 1959-1961, que Superior Glass Window déduisait de ses rapports d'impôt comme étant des frais d'exploitation, sommes dont le ministère du Revenu national réclame le remboursement de l'appelant.

Les parties, suivant consentement au dossier, ont soumis, comme ci-après relaté, leurs propositions de droit:

1. A qui appartiennent les améliorations et additions faites à l'immeuble loué au cours des années 1959 à 1961 inclusivement?
2. Si lesdites améliorations et additions appartenaient à l'appelant, à compter de quand lui ont-elles appartenu?
3. Si lesdites améliorations appartenaient à l'appelant, et si elles lui ont appartenu à compter du moment où elles ont été faites,
   a) Ont-elles donné lieu à une attribution de bénéfices ou avantages par la compagnie de l'appelant «en tant qu'actionnaire» au sens de l'article 8(1) de la Loi de l'impôt sur le revenu; ou
   b) Est-ce que le coût de ces améliorations doit être considéré comme faisant partie du coût de location desdits immeubles, et donc comme étant du revenu provenant d'un bien, d'une entreprise ou même d'une source quelconque, au sens des articles 3 et 4 de la Loi de l'impôt sur le revenu; ou
   c) Constituent-elles un avantage au sens de l'article 137(2)(*a*) de la Loi de l'impôt sur le revenu?

Les deux premières questions n'en font qu'une pour peu que l'on reconnaisse à l'appelant, ainsi que je dois le faire, la propriété des améliorations et additions à l'immeuble originel au fur et à mesure de leur accomplissement. L'article 415 du *Code civil de Québec* nous apporte dans les termes qui vont suivre une solution corroborative:

> 415. Toutes constructions, plantations et ouvrages sur un terrain ou dans l'intérieur sont présumés faits par le propriétaire, à ses frais, et lui appartenir . . .

(Les soulignés sont ajoutés.)

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Or, au paragraphe 2 de son Avis d'appel, St-Germain atteste son droit de propriété, spécifiant que:

> 2. Au cours des années d'imposition en question l'appelant a loué à un loyer annuel de $6,600 00 le terrain et la bâtisse dans laquelle la compagnie exerçait son entreprise

C'est une lapalissade de dire que la compagnie appartenait à ses actionnaires; en l'espèce, le pluriel n'est même pas de mise puisqu'il n'y avait qu'un seul et unique détenteur de tout le capital-actions, l'appelant. A toutes fins pratiques, St-Germain ne louait à nul autre qu'à lui-même.

La troisième et dernière proposition de droit, dans ses alinéas (a), (b) et (c), pose bien, il me semble, le seul et assez simple problème, celui que règlent les articles 8(1) alinéas (*b*) et (*c*) et 137(2) de la *Loi de l'Impôt sur le revenu.* Je joindrais à ces textes, *ex majore cautela,* l'article 12(1)(*b*) qui interdit, dans le calcul du revenu «la déduction d'une somme déboursée...à compte de capital ...». Est-il possible de concevoir des investissements de capitaux plus authentiquement tels que ceux dont fait mention l'Avis d'appel en son paragraphe 3(a), (b) et (c); je cite:

> 3. En raison de l'augmentation rapide du chiffre d'affaires de la compagnie, cette dernière améliora à ses frais les lieux loués comme suit:
> (a) Au cours de l'année 1959, la compagnie a construit un entrepôt au coût de $2,596.55;
> (b) Au cours de l'année 1960, la compagnie a construit un rajout à l'édifice au coût de $20,963 28;
> (c) Au cours de l'année 1961, la compagnie a de nouveau agrandi l'édifice au coût de $48,108.60.

L'emploi des verbes «construire et agrandir» démontre clairement que le bâtiment acheté en 1953, acquérait en 1961, des proportions beaucoup plus considérables que celles de naguère, consistant en des constructions immobilières de nature permanente qui augmentaient d'autant l'actif capitalisé de la compagnie.

Quant à l'alinéa (b) du paragraphe 3 des faits admis, je ne saurais y attacher la moindre importance. D'un simple bail verbal, au loyer annuel de $6,600.00, quel infime indice de preuve pourrait-on déduire qu'il comportât, additionnellement, l'écrasante charge d'effectuer, en trois ans, des constructions et améliorations au coût de $71,668.43? J'écarte d'emblée cette suggestion.

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Il me reste encore à considérer le sens conjugué des articles 8(1)(*a*)(*b*)(*c*) et 137(2)(*a*) de notre *loi fiscale*. Le premier édicte que:

> 8(1) Lorsque dans une année d'imposition,
>
> (*a*) un paiement a été fait par une corporation à un actionnaire autrement qu'en vertu d'une opération commerciale authentique,
>
> (*b*) des fonds ou biens d'une corporation ont été affectés de quelque manière que ce soit à un actionnaire ou à son avantage, ou
>
> (*c*) un bénéfice ou un avantage a été attribué à un actionnaire par une corporation, autrement
>
> (i) qu'à l'occasion de la réduction du capital, du rachat d'actions, ou de la liquidation, cessation ou réorganisation de son entreprise,
>
> (ii) qu'en payant un dividende sous forme d'actions, ou
>
> (iii) qu'en conférant à tous les détenteurs d'actions ordinaires du capital de la corporation un droit d'y acheter des actions ordinaires additionnelles,
>
> le montant ou valeur en l'espèce est inclus dans le calcul du revenu de l'actionnaire pour l'année.

Il n'est pas douteux que le sous-paragraphe (*c*) ci-dessus qualifie exactement le «bénéfice ou avantage» attribué par sa compagnie à son actionnaire-propriétaire, le favorisant d'une plus-value, de nature immobilière, qui permit à St-Germain de réaliser, le 9 août 1962, lors de la vente de sa fabrique, un profit net de $157,794.01. Mais, je le répète, la non-déductibilité des impenses annuelles, omises dans les rapports de Superior Glass Window Company, résulte initialement de l'interdiction décrétée à l'alinéa (*b*) de l'article 12(1) de la Loi (*supra*).

Enfin, l'article 137(2) prévoit l'inclusion «dans le calcul du revenu du contribuable» en l'occurrence, l'appelant, de toutes «opérations de quelque nature que ce soit...» ayant pour résultat «qu'une personne, ici la compagnie, confère un avantage» à ce contribuable. A maintes reprises, nous avons dit que de tels «avantages ou bénéfices» avaient été conférés à Charles-Édouard St-Germain.

Avec les commentaires et précisions que j'ai estimés opportuns, j'abonderais, entre autres, dans le sens de l'une des soumissions de l'intimé ainsi rédigée dans sa Réponse à l'Avis d'Appel:

> 3(g) A compter du parachèvement de chaque amélioration ou addition, il en résultait un accroissement de valeur au moins égal au montant des dépenses encourues pour telle amélioration ou addition, soit: $2,596.55; $20,963.28 et $48,108.60, pour les années 1959, 1960 et 1961 respectivement.

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Ces additions, dont la plus importante partie comprenait la construction de nouvelles bâtisses, augmentèrent le volume d'affaires de l'appelant, sous le truchement de sa compagnie, de l'ordre de $200,000, en 1954 à plus d'un million de dollars en 1961. Cette remarquable progression assura une appréciation adéquate à St-Germain qui, au mois d'août, 1962, vendait à la Maison Bienvenu Limitée, de Montréal, les 313 actions de Superior Glass Window au prix de $318,131, ainsi que «les terrains et immeubles dans lesquels cette compagnie opère», à un coût de $275,000, puis, encore, contre remboursement d'une somme de $56,869, «. . . avances qui me sont dues par Superior Window Co. Ltd. . . .», au total: $650,000, (pièce A-3).

Depuis l'audition, les parties ont produit des plaidoyers écrits, très élaborés et d'une rédaction limpide, auxquels ce m'est un agréable devoir de décerner des éloges mérités.

Puisque j'ai indiqué, ci-haut, mon sentiment favorable à la thèse de l'intimé, je me restreindrai à une brève analyse du plaidoyer de l'appelant, dont l'essentielle soumission de droit est ainsi posée à la première page de ce mémoire:

> . . . le nœud du débat se situe d'abord au niveau de la troisième question en litige . . . nous commenterons en premier lieu cette troisième question . . .
>
> TROISIÈME QUESTION EN LITIGE:
>
> Si lesdites améliorations appartenaient à l'appelant, et si elles lui ont appartenu à compter du moment où elles ont été faites,
>
> a) Ont-elles donné lieu à une attribution de bénéfices ou avantages par la compagnie à l'appelant «en tant qu'actionnaire» au sens de l'article 8(1) de la Loi de l'impôt sur le revenu;
>
> 1. Notre première proposition est celle-ci: l'article 8 de la Loi de l'impôt sur le revenu ne s'applique pas lorsque la compagnie a agi aux fins de ses affaires ou de son entreprise.

A l'appui de cette prétention les savants procureurs de l'appelant reproduisent de copieuses citations de l'instance: *M.N.R. v. Pillsbury Holdings Ltd.*[1], qui, à mon sens, traitait de conditions différentes et plutôt complexes, alors que l'actuel litige me semble d'une élémentaire simplicité.

Aux formulations précédentes, et pour leur donner leur exacte signification, il importe d'ajouter cette autre (Plaidoyer de l'Appelant, page 9):

> 6. . . . Nous soumettons, d'abord, à titre de principe de base, qu'en droit civil, faute de stipulations dans le bail, les améliorations locatives appartiennent au locataire qui les a fait construire à ses frais.

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[1] [1965] 1 R.C. de l'É. p. 676 et suivantes.

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Ainsi l'article 1640 du Code Civil se lit comme suit:

> 1640. Le locataire a droit d'enlever avant l'expiration du bail, les améliorations et additions qu'il a faites à la chose louée, pourvu qu'il la laisse dans l'état dans lequel il l'a reçue; néanmoins, si ces améliorations et additions sont attachées à la chose louée, par clous, mortier ou ciment, le locateur peut les retenir en en payant la valeur.

A ce point précis apparaît, à mon humble avis, la faiblesse sophistique de l'appel qui, dans les circonstances, voudrait établir une identité distincte entre la compagnie locataire et le locateur, alors que celui-ci est l'unique propriétaire de celle-là, de tout son capital-actions, et de chacun des immeubles qu'il «loue» verbalement à sa propre créature. Il va de soi que l'article 1640 règle le cas, tout autre, où locataire et locateur sont deux personnes distinctes. Telle est la réplique qu'oppose l'intimé à la page 4 de son Plaidoyer; je cite:

> Par ailleurs, l'Appelant soulève un argument fondé sur l'article 1640 du Code civil. Nous devons immédiatement suggérer à la Cour que cet article n'a pas d'application ici puisque, d'une part, il règle un moment de la vie des relations juridiques du locateur et du locataire, soit la fin du bail, et qu'il suppose clairement que le locateur et le locataire sont deux personnes différentes. Or, au cours des années en question (1959-1960-1961) le bail n'était pas terminé, et, lorsqu'il a pris fin, c'est par confusion, ce qui empêche toute opération de l'article 1640 C.c. dans les circonstances. D'autre part, avons-nous vu, l'Appelant n'ayant jamais renoncé à son droit d'accession, il devenait seul et unique propriétaire des améliorations au fur et à mesure qu'elles étaient complétées.

Pourrait-on comprendre, sans tomber dans l'absurde, que Superior Window Company, ne dépendant pas totalement de St-Germain, eut alors assumé une dépense de $71,668.43 pour des constructions sur un terrain loué au mois, sans autrement se prémunir contre l'application du droit d'accession du locateur, selon que stipulé aux articles 414, 415 et 1640 du *Code civil.*

Que la plus-value ainsi assurée aux immeubles de l'appelant, à même les revenus de sa compagnie, lui ait procuré un bénéfice et des avantages en sa qualité d'actionnaire, et actionnaire unique, «*qua* shareholder» selon l'expression consacrée, cela me paraît une irréfutable conclusion.

Ce bénéfice, qui, d'un même coup, avantageait la compagnie et son propriétaire, St-Germain, ressort de façon concise, des notes du savant membre de la Commission d'Appel de l'impôt, Me Maurice Boisvert, c.r. (voir pages 4 et 5 des motifs du jugement) qui écrit:

> Comme les bâtisses donnaient lieu à une allocation à l'égard du coût en capital desdites bâtisses, l'appelant réclamait cette allocation et

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en déduisait le montant de son revenu chaque année. En somme, d'une part, Superior Window payait pour améliorer et agrandir des propriétés immobilières qui ne lui appartenaient pas et en portait le coût au compte des dépenses d'opérations. D'autre part, l'appelant réclamait les allocations du coût en capital de ses biens immobiliers. La compagnie de l'appelant payait moins d'impôt et l'appelant, de son côté, payait aussi moins d'impôt. Ce peut être une manière habile de faire de bonnes affaires, mais la loi, dans sa sagesse, semble avoir prévu ce genre d'affaires en adoptant l'article 8 précité.

Par tous ces motifs, l'appel est rejeté. L'intimé aura droit de recouvrer ses frais après taxation régulière.

Toronto 1968 Apr. 26

BETWEEN:

MELNOR MANUFACTURING LTD. and MELNOR SALES LTD. .... PLAINTIFFS;

AND

LIDO INDUSTRIAL PRODUCTS LIMITED .... DEFENDANT.

Industrial design—Interlocutory injunction—Clear case of piracy—Validity of registration attacked—Balance of convenience, whether governing factor.

Defendant persisted in marketing a lawn sprinkler which was a virtual copy of plaintiffs after being informed of plaintiffs' recently registered industrial design. Upon plaintiffs' motion for an interlocutory injunction defendant attacked the validity of the registration on the grounds (a) that it was not original; (b) that the registration was not effected by the author or a person for whom the author executed the design; (c) that there was prior publication of the design in Canada and that a statutory requirement concerning marketings had not been complied with, and urged in consequence that on balance of convenience as between the parties the interlocutory injunction should not be granted. The Court rejected objections (a) and (c).

Held, an interlocutory injunction should be granted This being a clear case of piracy it was not to be determined on balance of convenience merely because defendant by objection (b) had raised some very tenuous argument that might lead to the invalidation of plaintiffs' title *Smith v. Grigg Ld* [1924] 1 K.B 655; *Bourjois Ld. v. British Home Stores Ltd* (1951) 68 R.P.C. 280, considered

APPLICATION for an interlocutory injunction.

James D. Kokonis for plaintiffs.

Weldon F. Green for defendant.

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JACKETT P. (orally):—This is an application for an interlocutory injunction restraining the defendant until the trial or other disposition of this action from infringing the plaintiffs' industrial design for a "rain sprinkler" as registered in the Register of Industrial Designs under No. 226/29037, and from applying to wares for the purposes of sale any design identical to or a fraudulent imitation of the said design and exposing for sale and selling such goods.

The Statement of Claim alleges that the plaintiffs and the defendant are Canadian companies, that, on January 30, 1967, an industrial design for a lawn sprinkler was registered in the Register of Industrial Designs under No. 226/29037 in the name of International Patent Research Corp., and was assigned, on March 28, 1968 to the plaintiffs; that, since the assignment the defendant had offered for sale to the public and sold lawn sprinklers identified by the defendant by the name of "Swinger", and not made by the plaintiffs or International Patent Research Corp., or with the licence of any of them, one of which sprinklers was attached to and made part of the Statement of Claim, and that the design applied to the sprinklers so offered for sale by the defendant was the plaintiffs' registered design or a fraudulent imitation thereof. No defence has been filed.

On the return of the application before me yesterday and today, in addition to hearing the application on the material filed by the plaintiffs—the defendant having filed no material—by special leave, Samuel Warshauer, an officer of each of the plaintiff companies as well as of International Patent Research Corp., appeared as a witness to supplement the information contained in an affidavit that he had taken and that is part of the plaintiffs' material and to be cross-examined.

It is conceded by counsel for the defendant that the sprinkler that was attached to and made part of the Statement of Claim was sold by the defendant in Canada and that the defendant is still selling sprinklers of which it is a sample.

The defendant, however, denies that the sprinklers in question have had applied to them either the plaintiffs' registered design or a fraudulent imitation thereof. The defendant also attacks the validity of the registration of the plaintiffs' design

(a) on the ground that it was not original,

(b) on the ground that the registration was not effected by the author or a person for whom the author executed the design,

(c) on the ground that there was prior publication of the design in Canada more than one year before its registration and that the section 14 requirement concerning markings had not been complied with.

The defendant's position is that there are serious issues to be decided on the trial of the action and that, having regard to the balance of convenience as between the parties, the interlocutory injunction sought should not be granted.

The plaintiff companies are wholly owned subsidiaries of a United States company and are part of a family of companies known as the "Melnor family" engaged in the business of manufacture and sale of garden hose accessories, including lawn sprinklers. Other companies in the family carry on such a business in the United States and the plaintiffs carry on such a business in Canada. Some of the goods sold in Canada are manufactured in Canada, some are imported from the United States. In addition to the companies engaged in active business, International Patent Research Corp. is a member of the family that was incorporated to hold all patent rights of the Melnor family.

In 1966, the Melnor family, finding itself faced with competition in the United States with a low-priced sprinkler, engineered a new, inexpensive sprinkler to meet such competition and had a design created for such new model by an independent industrial designer of New York City, John D. Blinert. They sold that sprinkler during the 1966-67 season in the United States and then withdrew it from the market because the low-priced competitor had disappeared from the market and because they found that their low-priced model yielded them very little profit, while it reduced their sales of more expensive models that yielded them better profits.

That low-priced model, which was identified by the Melnor family as "RAIN-WAVE No. 33", was not sold by the Melnor family in Canada because they had not met the same low-priced competition here. Nevertheless, the design applied to RAIN-WAVE No. 33, which, as I have said, was created for the Melnor family by a professional designer, was registered in Canada by International Patent Research Corp. on January 30, 1967.

Early in 1968, it was found that the defendant was using sprinklers of the Melnor family's manufacture under the "RAIN-WAVE No. 33" designation as models for seeking orders in Canada for the sale of sprinklers. It appeared that, before using them in that way, the defendant had removed the Melnor identification from the sprinklers and had substituted their own name. This was done by grinding off Melnor's name where it was embossed on the sprinklers and by placing over the place where it was a sticker with the word "Lido" on it. The defendant was at that time offering to sell such sprinklers under the trade mark "SWINGER".

When the Melnor family discovered this activity on the part of the defendant, a lawyer's letter was written on their behalf to the defendant advising of the Industrial Design Registration in question. That letter was dated January 22, 1968.

In March 1968 there came into the hands of the Melnor family a sample of a sprinkler bearing the defendant's name that was, practically speaking, exactly the same as the Melnor family's "RAIN-WAVE No. 33" and that had *not* been manufactured by any of the Melnor family.

While proceedings had been begun earlier in this Court in the name of International Patent Research Corporation, the registered owner of the industrial design, and one of the present plaintiffs, on advice of their Canadian lawyers, the registration was assigned to the plaintiffs, the Canadian members of the Melnor family, on March 28, 1968, and the first action was discontinued.

Before that first action was discontinued, there was brought to the attention of the plaintiffs the sprinkler (as exemplified by the sprinkler that was made part of the Statement of Claim herein) which the defendants are now producing and selling in Canada. That sprinkler is marketed under the name "SWINGER" and is a reproduction of

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the "SWINGER" produced prior thereto by the defendants (which, as I have said, is an exact reproduction of the plaintiffs' sprinkler to which their registered design has been applied) except that three walls of each end of the sprinkler have been given a shallow "V" effect instead of that of a straight line, or a shallow concave effect.

In those circumstances the plaintiffs launched the present action on April 19, 1968, and launched the present application for an interlocutory injunction.

In the first place, I reject the submission that there has been undue delay on the part of the plaintiffs in bringing the present application. Having regard to the unavoidable time lapses in the conduct of litigation and in communications among persons resident in several different cities, the time lapse does not seem to me to be undue, and certainly the defendant has not brought any evidence to show any prejudice resulting therefrom.

With regard to the question of infringement, in my view, the plaintiff has made out a very strong *prima facie* case that the defendant has, contrary to section 11 of the *Industrial Design and Union Label Act,* R.S.C. 1952, chapter 150, without the licence in writing of the registered proprietor or of his assignee, applied for the purposes of sale "a fraudulent imitation" of the registered design, if it has not applied the registered design itself, to the ornamenting of its sprinklers. Furthermore, it has done so, and persists in doing so, some time after it has been formally advised of the plaintiffs' registered design. In the absence of any evidence or explanation from the defendant, I can only conclude that the defendant was guilty of unashamed appropriation of the plaintiffs' legal rights or that it was under the impression that the minor changes it made in the course of appropriating the plaintiffs' design were sufficient to convert that design into a new and different design, a point of view I find it impossible to appreciate. I have examined a sprinkler to which the registered design has admittedly been applied and the defendant's sprinkler that is part of the Statement of Claim from every different angle and, apart from a direct head-on view, their similarity is, in my view, incontrovertible. Even from a direct head-on view, the defendant's sprinkler is an obvious adaptation of the plaintiffs'.

Turning to the question of validity, I have no difficulty in holding that the defendant has not made out a case that raises any real question in my mind as to the originality of the plaintiffs' registered design. The various earlier sprinklers relied on are all the same kind of sprinkler. The designs used to ornament those various sprinklers are, however, in my opinion, each quite different from the plaintiffs' registered design.

So far as the attack based on section 14 of the Act is concerned, I find that no facts have been established to support it. I do not find any publication of that design in Canada before it was registered and I do not find that sprinklers to which the design had been applied were sold or offered for sale in Canada without the markings required by section 14. I make no comment on what the result would have been if such facts had been established.

Finally, the defendant put forward a contention that the registration was invalid because, the registration had not been effected by either the author or the person for whom the author had created it, but, rather, by some person to whom the latter company had assigned the design before it was registered. While I can see that it is not inconceivable that this contention might prevail after full argument, superficially at least, it is met by the fact that a design exists before registration, and section 13 of the Act provides that "Every design is assignable in law".

I have in mind, of course, the long established practice in patent matters that an interlocutory injunction will not ordinarily be granted on the basis of a recent patent where there is a genuine case to be decided as to its validity.[1] I realize that, in an appropriate case, this practice is applicable in industrial design matters. I should, however, be very hesitant about applying that practice in an industrial design case where there is, as I am convinced there is here, a clear case of appropriation by the defendant of the plaintiffs' industrial design which, I must assume, is ordinarily a valuable property acquired at some expense as other property is acquired, knowing that he is appropriating something to the exclusive use of which, by virtue of an Act of Parliament, the plaintiff has a duly registered title; and, I am none the less hesitant about applying the prac-

[1] Compare *Smith v. Grigg Ld.* [1924] 1 K.B. 65.

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tice because the defendant has managed to raise some very tenuous arguments based upon an interpretation of the statute that possibly might lead to the invalidation of the title. I find some support for the view that I take of the matter in *Bourjois Ld. v. British Home Stores Ld.*[2] per Lloyd-Jacob J. at pages 281-2:

> The first thing that is urged upon me by the Defendants is this, that having regard to the recent date of this registration and to the fact that the Defendants assert that they do propose to challenge the validity of this registration, the practice of this Court is such as not to grant any interlocutory injunction.
>
> In support of that, I have been referred to the decision in *Smith v. Grigg Ld.* (1924) 41 R.P.C. 149. That was an interlocutory appeal coming before *Scrutton* and *Atkin,* LL. JJ., in an action commenced in the King's Bench Division, but which was in respect of an alleged infringement of a registered design. The learned Judge in Chambers appears to have granted an interlocutory injunction, and the matter came before the Court of Appeal. According to the report, the case was very fully argued by distinguished Counsel, and in the result the learned Lords Justices came to the conclusion that a practice which was admitted to be common in respect of Letters Patent should also be adopted in respect of registered designs, and that where a monopoly sought to be enforced by injunction was of comparatively recent date, the burden on the plaintiff was to satisfy the Court on motion that there was sufficient probability of success in establishing his *prima facie* right as would make it proper to protect that right by interlocutory injunction.
>
> It is the fact, as I observed in argument, that the practice both in respect of applications for Letters Patent and for registered designs has undergone some modification since the time when the Court of Appeal were considering that matter, and it does not seem to have been argued in that case that, particularly as regards registered designs, the novelty of design is that which in general causes it to be of value in commerce, and that therefore its value in the early period of its novelty might well be regarded as being greater than the residue of the novelty after its initial impact on the market has disappeared. I find that that principle has in fact been applied in subsequent applications and it would only be for very compelling reasons that I could find myself free to differ in a matter of practice now so well established, but I think it is right that I should say that it may well be that in a proper case the practice may require to be reconsidered and if, as is possible, I should find myself bound by a decision of the Court of Appeal it might be necessary so to express the judgment of this Court as to permit the matter readily and easily to be reviewed in a higher Court.

and per Evershed, M.R. at page 284:

> It was said by Mr. Shelley that the learned Judge was over influenced by the case of *Smith v. Grigg Ld.* in which *Scrutton* and *Atkin,* LL. JJ., had suggested that in the case of a new patent, and, therefore, of a new design, it was not the practice of the Court to

[2] (1951) 68 R.P.C. 280.

grant an interlocutory injunction except in very exceptional cases. *Lloyd-Jacob, J.*, observed that since that case the practice has somewhat altered, and he drew attention to the fact that with a design newness and novelty may be of the very essence of the right of the Plaintiff. I do not think it right to say that *Lloyd-Jacob, J.*, was deterred by that case, as I read his judgment, from doing what he would otherwise have thought it right to do. I share his view that this point is one of difficulty and therefore I should myself, apart from anything else, see no ground for interfering with his discretion.

This being a case of piracy of the plaintiffs' rights without colour of right, it is not a case, in my view, where the granting of an interlocutory injunction depends upon balance of convenience.

I have not overlooked the fact that the plaintiffs have had no intention of using their registered design in Canada except to meet competition in the inexpensive sprinkler field such as that that they are now encountering from the defendant. That may be, from many points of view, unfortunate. I must, however, take the statute as I find it. Parliament did not impose conditions relating to user on the ownership of registered designs such as those to be found in the *Patent Act*.

There will be an injunction as sought and I will hear submissions as to the form that it should take.[3]

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[3] The pronouncement read as follows:

Let an injunction go restraining the defendant by itself, its officers, servants or agents, until disposition of this action after trial or other disposition of this action, from applying to any articles for the purpose of sale

(a) the design registered under No. 226/29037 in the Register of Industrial Designs;

(b) the design applied to the end supports of the sprinkler that is referred to in the statement of claim herein as being filed therewith as Schedule "B" thereto, or

(c) any other imitation of the said registered design,

and from selling or exposing for sale or use any article to which any such design has been applied.

Order to contain usual undertaking by the plaintiffs.

Costs in the cause.

Toronto 1968 Apr. 18 — Ottawa May 3

BETWEEN:

THE NOXZEMA CHEMICAL COMPANY OF CANADA LIMITED .... APPLICANT;

AND

SHERAN MANUFACTURING LIMITED and WILLIAM SOROKOLIT RESPONDENTS.

Trade Marks—Application to expunge for abandonment—Whether prohibited—Previous proceeding before Registrar to explain non-user—Trade Marks Act, ss. 44, 56(1) and (2).

In a proceeding instituted by Noxzema Chemical Co. under s. 44 of the *Trade Marks Act* the registered owner of the trade mark "Blem" accounted for its non-user for a period of years as being due to the necessity of research to find a solution for the instability of the product with which the mark was associated. The Registrar thereupon decided that absence of use was due to special circumstances, and on the strength of further evidence furnished in response to a second notice by the Registrar under s. 44 decided that the mark was then in use in Canada. The Noxzema Company did not appeal from either decision, and subsequently applied under s. 56 of the *Trade Marks Act* to expunge the trade mark on the ground (*inter alia*) that it had been abandoned.

Held, such application did not call into question either of the Registrar's decisions and so was not barred by s. 56(2). The Registrar had no jurisdiction under s. 44 to adjudicate the question of abandonment.

Smit v. Packsack [1964] Ex. C.R. 226, referred to.

Roy H. Saffrey for applicant.

N. M. S. Johnston for respondents.

APPLICATION.

JACKETT P.:—In this application, by way of originating Notice of Motion dated March 18, 1968, under section 56 of the *Trade Marks Act* for an order expunging from the Register of Trade Marks the registration of a particular trade mark, a question was set down for determination before the hearing of the expungement application as to whether, having regard to the facts set out in a statement of facts agreed to by counsel for the parties, the applicant was prohibited by subsection (2) of section 56 of the Act from instituting the expungement proceedings in whole or in part.

The application for expungement of the trade mark was based on two alternative grounds, *viz.*:

(a) the original registrant was not entitled to registration, and

(b) the trade mark has been abandoned.

The respondents' position on the preliminary question of law is that, by reason of the facts agreed upon, the applicant is prohibited by section 56(2) of the *Trade Marks Act* from instituting these proceedings in so far as they are based upon the contention that the trade mark has been abandoned.

The agreed Statement of Facts reads as follows:

1 On November 1, 1966 the respondent WILLIAM SOROKOLIT was the registered owner of Registration No. 113,912, registered on April 24, 1959 for the trade mark "BLEM" in association with a medicated face lotion and an abrasive cleanser for the treatment of acne.

2. By an assignment dated September 11, 1967, and registered in the Trade Marks Office on January 18, 1968 the said registration was assigned to the respondent SHERAN MANUFACTURING LIMITED.

3. The applicant THE NOXZEMA CHEMICAL COMPANY OF CANADA LIMITED applied to register "THERA-BLEM" as a trade mark by way of application Serial No. 298,040, on June 25th, 1966.

4. The Trade Marks office has informed the applicant, THE NOXZEMA CHEMICAL COMPANY OF CANADA LIMITED, that "THERA-BLEM" the subject of the said application Serial No. 298,040 does not appear to be registrable inter alia because of Registration No. 113,912 for the trade mark "BLEM".

5. On November 1, 1966, the applicant, THE NOXZEMA CHEMICAL COMPANY OF CANADA LIMITED through its agents, Fetherstonhaugh & Co., 443 University Avenue, Toronto, requested the Registrar of Trade Marks to give notice to the registered owner of the trade mark "BLEM" Registration No. 113,912 under the provisions of Section 44(1) of the *Trade Marks Act*.

6. On November 15, 1966 the Registrar of Trade Marks sent a notice, pursuant to the provisions of Section 44(1) of the *Trade Marks Act*, to the registered owner, WILLIAM SOROKOLIT.

7. The registered owner, the respondent WILLIAM SOROKOLIT, furnished the Registrar of Trade Marks with an affidavit, pursuant to the aforesaid Notice, in which he swore, inter alia, that:

> "2. I began to use the trade mark BLEM in Canada for the said wares in 1959, the wares being an emulsified lotion and cleanser sold in bottles. It was found that, although the product was effective in the treatment of acne, the emulsion was unstable, with the result that after a time the product in the bottles formed lumps or caked. Because of this problem I discontinued the sale of the product in 1959 until the problem could be solved.

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3. My business has always been a modest one-man business. I sell products that are distributed through drug stores, beauty parlors and barber shops. Because my business is a small one I am unable to have research facilities of my own and I must depend on the part time help of others for scientific investigations. When I encountered the problem that the emulsion of my BLEM lotion was breaking I asked one of my friends, Dr. James Salter, Ph.D. (Biochemistry), and subsequently Mr. Leonard Wineberg, a formulating chemist, both of Toronto, to attempt to solve the problem so that I could market the product successfully. Their work has continued since 1959, encouraged by continuing evidence of the efficacy of the product in treating acne. Mr. Wineberg's efforts have finally resulted in a composition that is currently undergoing tests for shelf life, and the results have been sufficiently promising to justify the preparation of a fresh packaging design.

4. It is only because of the special circumstances set forth in paragraph 3 that my trade mark BLEM has not been recently in use in Canada, and I have never intended to give up or abandon the mark. Prior to my adoption of the mark BLEM I had considered several other trade marks for which my trade mark agents made searches at the Trade Marks Office, but none of these earlier marks appeared to be free of conflict with marks already registered. I thus have expended considerable time and money in selecting and registering the mark, it has always appealed to me as a good mark for the wares in question, and it has always been my intention to resume using it for my product as soon as my difficulties with the emulsion were overcome. In view of Mr. Wineberg's work I expect to be able within the next few months to resume the use of the mark in Canada for the wares for which it is registered, and my sole reason for not having done so before now is that I wish to ensure that the goods sold in association with it are satisfactory from all points of view."

8. No representations were made to the Registrar by or on behalf of the registered owner of the trade mark or by or on behalf of the applicant at whose request the notice referred to in paragraph 6 was given.

9. On March 29, 1967, the Registrar of Trade Marks gave notice to the applicant, through its above named agents as follows:

"Re: Registration No. 113,912 'BLEM'

At your request a notice under the provisions of Section 44 wâs issued against the above-described trade mark.

The evidence submitted has been considered and I am satisfied that absence of use has been due to Special circumstances. For this reason, a second notice under Section 44 will be directed against the above trade mark in six months."

10. On March 29, 1967, the Registrar of Trade Marks gave notice to the registered owner, WILLIAM SOROKOLIT in substantially the same terms.

11. On October 4, 1967, the Registrar of Trade Marks sent a further notice pursuant to section 44 of the *Trade Marks Act* to the registered owner, the respondent WILLIAM SOROKOLIT.

12. The registered owner, the respondent, WILLIAM SOROKOLIT furnished the Registrar of Trade Marks with a statutory declaration, pursuant to the aforesaid notice, in which he declared, that:

"1. THAT I am the President of Sheran Manufacturing Limited, the owner of the trade mark BLEM the subject of Canadian trade mark registration number 113,912, and as such have knowledge of the facts hereinafter set forth.

2. THAT on the 28th day of September, 1967, Sheran Manufacturing Limited, as my assignee, resumed the sale in Canada of medicated face lotion and an abrasive cleaner for the treatment of acne, using the trade mark BLEM for such wares.

3. THAT attached hereto is a label which Sheran Manufacturing Limited is using for the aforesaid wares."

13. No representations were made to the Registrar of Trade Marks by or on behalf of the registered owner of the trade mark or by or on behalf of the applicant at whose request the notice referred to in Paragraph 11 was given.

14. On February 1, 1968, the Registrar of Trade Marks gave notice, to the applicant, through its agents Fetherstonhaugh & Co., 443 University Avenue, Toronto, and to the registered owner, the respondent, SHERAN MANUFACTURING LIMITED, of his decision with respect to Registration No. 113,912 for the trade mark "BLEM" in the following terms:

"The affidavit submitted in connection with the registration has been considered.

I am satisfied that the evidence submitted establishes that the trade mark is in use in Canada in association with the wares specified in the registration. In the circumstances, it is my decision not to amend or expunge the registration."

15. No appeal has been taken from any decision of the Registrar of Trade Marks within the time limited by the *Trade Marks Act*.

16. There has been no communication between the applicant herein and the Registrar of Trade Marks other than the foregoing.

The relevant provisions of the *Trade Marks Act* read as follows:

18. (1) The registration of a trade mark is invalid if

* * *

(*c*) the trade mark has been abandoned;

* * *

44. (1) The Registrar may at any time and, at the written request made after three years from the date of the registration by any person who pays the prescribed fee shall, unless he sees good reason to the contrary, give notice to the registered owner requiring him to furnish within three months an affidavit or statutory declaration showing with respect to each of the wares or services specified in the registration, whether the trade mark is in use in Canada and, if not, the date when it was last so in use and the reason for the absence of such use since such date.

(2) The Registrar shall not receive any evidence other than such affidavit or statutory declaration, but may hear representations made by or on behalf of the registered owner of the trade mark or by or on behalf of the person at whose request the notice was given.

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(3) Where, by reason of the evidence furnished to him or the failure to furnish such evidence, it appears to the Registrar that the trade mark, either with respect to all of the wares or services specified in the registration or with respect to any of such wares or services, is not in use in Canada and that the absence of use has not been due to special circumstances that excuse such absence of use, the registration of such trade mark is liable to be expunged or amended accordingly.

(4) When the Registrar reaches a decision as to whether or not the registration of the trade mark ought to be expunged or amended, he shall give notice of his decision with the reasons therefor to the registered owner of the trade mark and to the person at whose request the notice was given.

(5) The Registrar shall act in accordance with his decision if no appeal therefrom is taken within the time limited by this Act or, if an appeal is taken, shall act in accordance with the final judgment given in such appeal.

* * *

55. (1) An appeal lies to the Exchequer Court of Canada from any decision of the Registrar under this Act within two months from the date upon which notice of the decision was despatched by the Registrar or within such further time as the Court may allow, either before or after the expiry of the two months.

(2) The appeal shall be made by way of notice of appeal filed with the Registrar and in the Exchequer Court of Canada.

(3) The appellant shall, within the time limited or allowed by subsection (1), send a copy of the notice by registered mail to the registered owner of any trade mark that has been referred to by the Registrar in the decision complained of and to every other person who was entitled to notice of such decision.

(4) The Court may direct that public notice of the hearing of the appeal and of the matters at issue therein be given in such manner as it deems proper.

(5) On the appeal evidence in addition to that adduced before the Registrar may be adduced and the Court may exercise any discretion vested in the Registrar.

56 (1) The Exchequer Court of Canada has exclusive original jurisdiction, on the application of the Registrar or of any person interested, to order that any entry in the register be struck out or amended on the ground that at the date of such application the entry as it appears on the register does not accurately express or define the existing rights of the person appearing to be the registered owner of the mark.

(2) No person is entitled to institute under this section any proceeding calling into question any decision given by the Registrar of which such person had express notice and from which he had a right to appeal.

The respondents' contention is in effect, as I understand it, that, by what was done under section 44, the Registrar determined that the registered trade mark was being "used", that it was necessary for the applicant to establish that the trade mark was not being used to support his application for expungement in so far as it is based on abandonment, that the applicant was a person who had express notice of the Registrar's decision and who had a right to appeal therefrom, and that the applicant was therefore prohibited by section 56(2) from launching a proceeding under section 56 that was based on abandonment of the trade mark because any such proceeding necessarily called in question the Registrar's decision that the trade mark was being "used".

The applicant resists the contention that section 56(2) operates to prohibit some part of its application to expunge on two grounds, *viz.*:

(a) the application to expunge does not call into question any decision of the Registrar, and

(b) the applicant had no right to appeal from the decisions of the Registrar upon which the respondents rely as bringing into play section 56(2).

To reach a conclusion on the matter it is necessary to review section 44 of the *Trade Marks Act* and what happened under that section in this particular matter.

As I understand section 44(1), it provides for a notice being sent to the registered owner of a trade mark in two classes of case, namely, in a case where the Registrar himself has decided to do so, and in a case where a person who has paid a prescribed fee has made a request that the notice be sent. Such a notice is sent by the Registrar to the registered owner of a trade mark and requires the registered owner to furnish an affidavit or statutory declaration showing:

(a) whether the trade mark is in use in Canada, and

(b) if the trade mark is not in use in Canada,

  (i) the date when it was last so in use, and

  (ii) the reason for the absence of such use since such date.

Section 44(2) prohibits the Registrar from receiving any evidence other than the affidavit or statutory declaration furnished by the registered owner under section 44(1), but it expressly provides for the Registrar hearing representations made by or on behalf of the registered owner or by or on behalf of the person at whose request the notice was given. This provision makes it clear, in my view, that section 44 does not contemplate a determination of an

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issue as to whether a trade mark has been abandoned but is merely a procedure for clearing the Registry of registrations where there is no real claim by the registered owner that he has not abandoned the trade mark.

Section 44(3) does not provide for anything to be done by the Registrar or by any other person. It creates a substantive rule. It provides that the registration of a trade mark that has been the subject matter of a notice under section 44(1) is "liable" to be expunged or amended where, by reason of the affidavit or statutory declaration furnished by the registered owner, or the failure to furnish such evidence, it appears to the Registrar

(a) that the trade mark is not, either with respect to all the specified wares or service or with respect to any of them, in use in Canada, and

(b) that the absence of use has not been due to special circumstances that excuse such absence of use.

Section 44(4) contemplates the Registrar reaching a "decision" as to whether or not the trade mark "ought" to be expunged or amended in accordance with the rule created by section 44(3) and provides that, when he has reached that decision, he shall give "notice of his decision" with the reasons therefor to the registered owner and to the person at whose request the notice was given.

Section 44(5) requires that the Registrar "shall act in accordance with his decision" if no appeal therefrom is taken within the time limited by the Act, and that, if an appeal is taken, he "shall act in accordance with the final judgment given in the appeal". In other words, if the "decision" contemplated by section 44(4) is that the trade mark "ought" to be "expunged" or "amended" and there is no appeal within the prescribed time, the Registrar is to expunge or amend in accordance with his "decision" and, if there is an appeal, the Court's judgment is to tell him whether he is to expunge or amend.

As I read section 44, it does *not* provide a summary procedure for determining whether a registered trade mark has been "abandoned" within the meaning of section 18(1)(*c*). What it does, as I understand it, is provide a summary procedure whereby the registered owner of a trade mark is required to provide either *some evidence*

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that the registered trade mark is being used in Canada or evidence of "special circumstances that excuse...absence of use". The penalty for the registered owner failing to provide such evidence is that his trade mark becomes liable to be "expunged" (section 44(3)), and will be expunged (section 44(5)). What seems to be contemplated is that there will be on the Registry many trade marks that the registered owners do not use and in respect of which the registered owners make no pretence of having any interest. A notice under section 44(1) will obviously result in many of such trade marks being expunged because the registered owners will not respond to the notices or will furnish evidence that shows neither user nor anything that could be regarded, from the point of view of continued interest in the trade marks, as "special circumstances that excuse such absence of use". The fact that the Registrar is prohibited by section 44(2) from receiving any evidence other than that provided by the registered owner shows that it was not intended that the Registrar reach a "decision" under section 44 as to whether the registered owner had "abandoned" his trade mark or, indeed, whether the mark was in fact in use in Canada. What the Registrar decides is whether "by reason of the evidence furnished to him or the failure to furnish such evidence", it "appears to him" that the trade mark "is not in use in Canada" and whether, by reason of such evidence, it appears that the absence of use has not been due to special circumstances that excuse such absence of use.

To put it another way, section 44 provides a means for clearing from the Registry registrations for which the owners no longer assert that there is any real foundation. An owner can avoid having any action taken against his registration by either a mere declaration of user or, if he admits non-user, by any reasonable explanation therefor.

In this case, as appears from the facts agreed upon, the Registrar sent a notice at the request of the applicant to the second respondent when he was the registered owner of the trade mark in question and he came to the conclusion on the evidence furnished at that time "that absence of use has been due to special circumstances". The Registrar then sent a second notice under section 44(1) apparently of his own motion, and was then furnished with evidence by the first respondent, who had in the meantime become the

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registered owner, which "satisfied" him that the trade mark was "in use in Canada". He therefore decided not to amend or expunge it.

In my opinion, this application under section 56 of the *Trade Marks Act* to expunge the trade mark that was the subject matter of those notices does not call "in question" either of those two decisions made by the Registrar. Compare *Smit v. Packsack*[1] where Thurlow J. had what in my opinion was a very similar problem under section 56(2). The Registrar, in this case, made the decision required by section 44 on the evidence before him, which evidence, by reason of the particular purpose of section 44, was of a very limited character. He had no jurisdiction to conduct a hearing into the question as to whether the trade mark had been abandoned. He could not have received all available evidence on that question because section 44(2) prohibited him from doing so. He was not even deciding whether the evidence he could receive showed abandonment. He had to decide, in effect, whether the registered owner put forward a claim, supported by an affidavit or statutory declaration, to user in Canada or to circumstances that excused non-user. Having concluded that he was making such a claim, that was the end of the matter under section 44. In my view, after such a decision under section 44, any person who has an interest in raising a case of abandonment must do so in some such way as that adopted by the applicant in these expungement proceedings.

Having regard to the conclusion that I have reached, I need not consider whether the applicant had a right of appeal from the Registrar's decision under section 44.

There will be judgment answering the question raised in the negative. The costs related to having the question of law decided before trial, which are hereby fixed at $250, are costs to the applicant in the cause.

Before parting with the matter, I should say, so as to avoid misunderstanding in the future, that, in so far as the order setting the question down for hearing before trial was worded as though what was being ordered was a trial of an issue of fact, I was in error in making the order in that form. No harm, however, results from this oversight as it is quite clear, I think, that the order was intended to be an order under Rule 151 raising a question of law for the opinion of the Court by special case.

[1] [1964] Ex C R 226

Toronto 1968
Mar. 15
Ottawa May 3

BETWEEN:

DR. EDWARD GORDON MURPHY ......APPELLANT;

AND

THE MINISTER OF NATIONAL REVENUE .... RESPONDENT.

Income tax—Doctor's wife employed by office management company—Wife's services rendered husband—Whether remuneration deductible—Wife employee of husband—Artificial reduction of income—Income Tax Act, s. 21(2), 137(1).

Prior to 1963 appellant, a medical doctor, paid his wife $250 a year for attending to his office needs as receptionist and his bookkeeping work while at home. In 1963 appellant made an arrangement with his wife and accountant, with a view to avoiding taxes, for the provision of his receptionist, accounting, management and stenographic services for $500 a month by a company controlled by his accountant. That company in turn employed appellant's wife at $465 a month to perform the above services for appellant and kept $35 a month for performing the services which the accountant had previously performed. Appellant's wife deposited her monthly remuneration in her husband's bank account.

Held, the $6,000 paid the company in 1963 pursuant to the above arrangement was prohibited from deduction in computing appellant's income (1) under s. 21(2) of the *Income Tax Act* as being remuneration paid by appellant to his wife as his employee, and (2) under s. 137(1) as being an expense in respect of a transaction or operation that would unduly or artificially reduce his income.

INCOME TAX APPEAL.

Wolfe D. Goodman and *Arnold L. Cader* for appellant.

J. R. London for respondent.

DUMOULIN J.:—Dr. Edward Gordon Murphy, a Toronto medical practitioner, hereby appeals from a decision of the Tax Appeal Board, dated February 3, 1967[1], dismissing his initial appeal from an assessment made by the respondent, March 29, 1965, wherein, *inter alia,* an attempted income tax deduction of $6,000, for taxation year 1963, was disallowed.

The grounds alleged by appellant to justify the abovementioned deduction are that, in January 1963, he commissioned a local organization, by the name and style of Nexus Corporate Services Limited, to provide his professional

[1] [1967] Tax A.B.C. 132

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administrative requirements with regular receptionist, accounting, office management and stenographic services for a monthly fee of $500; that these ministrations, being duly procured during 1963, he paid Nexus the stipulated price of $6,000, deducting the said sum from his income returns "as an expense of carrying on his medical practice". Respondent refused to countenance this claim for the reasons stated in paragraphs 8 and 9, hereafter quoted, of the reply to the notice of appeal:

> 8. The respondent submits that the sum of $6,000 00 paid to Nexus Corporate Services was remuneration for services performed by his wife as an employee of the Appellant and the deduction of which, in computing his income, was prohibited by subsection (2) of Section 21 of the Income Tax Act.
>
> 9. The respondent further submits that the payment of the said sum of $6,000.00 to Nexus Corporate Services was a disbursement or expense made or incurred in respect of a transaction or operation that, if allowed, would unduly or artificially reduce the Appellant's income and therefore, the deduction of the said sum in computing the Appellant's income is prohibited by subsection (1) of Section 137 of the Income Tax Act, R.S.C. 1952, Chapter 148.

The evidence adduced in Court revealed that, prior to 1963, as testified to by the appellant, Dr. Murphy, his wife, born Nadia Kamil, of Egyptian extraction, attended to his office needs as a receptionist, performing also "a good deal of the bookkeeping work when at home". The Doctor adds, but rather unconvincingly, that "a regular receptionist was often employed to fill in the gap during his absence on calls at the hospital, a matter of some three hours daily". If so, I do not remember being given the names of any of those would-be "regular employees", and nothing dispelled my impression that Appellant's wife fulfilled most of the daily tasks associated with a medical office for a nominal compensation of $250 per annum.

Dr. Murphy next proceeds to explain that the agreement eventually concluded with Nexus Corporate Services, as outlined in Exhibit 1, a typewritten letter, dated November 26, 1962, on the above firm's stationery, addressed to "Nadia" and signed "Ted", "was an attempt to properly evaluate Mrs. Murphy's services". At all events those services, after due consultation between the three persons concerned, to wit: Dr. Murphy, his wife Nadia Kamil Murphy, and Edward William Imrie, Chartered Accountant, owner of Nexus Corporate Services Limited, were set at no less than $500 per month to be paid by the appellant to Nexus who, in turn paid back, each month, $465 to "Nadka Services" a puerile effort to transmute Mrs. Murphy's cheque receiving hands into some sort of company cash register. Unincorporated, unregistered and unknown, the so-called "Nadka Services" are devoid of all legal existence and, if I may slip into journalistic parlance, utterly fail to serve even as a mini-screen for Mrs. Murphy's personality.

Reverting now to reality, the monthly sum of $35 retained by Nexus, out of each $500 instalment received from the appellant, compensated "Ted" Imrie for the preparation of Dr. Murphy's income tax returns and some occasional accountancy work, as he was in the habit of doing for this client.

Edward William Imrie, a chartered accountant, the second witness heard, is, to all appearances, a close friend of the Murphys. He repeats, what we already knew, that Nexus Corporate Services had contracted to provide Dr. Murphy with receptionist, accounting, office management and stenographic services, at the above-stated remuneration of $500 monthly, entailing a corresponding refund of $465 to "Nadka Services".

This witness agrees he recommended the contract entered into by Nexus and Nadka Services "as a way or manner of avoiding income tax in connection with Dr. Murphy's office services and administration".

Most of this repetitious information appears in Exhibit 2, a letter of April 30, 1963.

This communication assumes a business style and is obviously meant to implement the innocuous scheme devised by the three participants. Its tone is formal, it is no longer addressed to "Nadia", nor signed "Ted"; I quote:

> Dr. E. G. Murphy,
> 3 Cumberland Drive,
> Port Credit, Ontario.
>
> Dear Mr. Murphy:
>
> Pursuant to our verbal agreement of January, wherein Nexus Corporate Services Limited agreed to provide the following services:
>
> Receptionist, accounting, office management and stenographic services
>
> for your practice, the trial period discussed has been completed. I am satisfied that the work is being done properly by the *agent* (em-

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phasis, mine) we have contracted with to do the work. If you are satisfied with the arrangement would you be good enough to forward fees covering the trial period ($500 × 4 months).

Yours very truly,

Nexus Corporate Services Limited
E. W. Imrie,
President.

A single remark suffices to focus Ex. 2 in its appropriate light. After some probing Dr. Murphy admitted that the expression "agent" in the text above "could well qualify his wife, Nadia"; and so it did.

For duty's sake, I would note Dr. Murphy's mention that, during 1963, his wife's daily attendance at the office was more frequent and for longer periods than previously. Mrs. Murphy stated, in turn, that the sums reimbursed to her by Nexus were, eventually, turned over to her husband's bank account "in order to avoid risk of double taxation", apparently in pardonable oblivion that section 21(2) of the *Act* had thoughtfully averted all such duplication.

It now remains to cite the two sections of the pertinent law which, in keeping with the proven facts, superabundantly dispose of the case. Section 21(2) enacts that:

> 21(1) . . .
>
> (2) Where a person has received remuneration as an employee of his (or her) spouse, the amount thereof shall not be deducted in computing the spouse's income and shall not be included in computing the employee's income.

We know the roundabout workings of the little play: Nexus hires appellant's wife to do administrative work in her husband's office; the latter performs the ostensible gesture, each month, of paying $500 to Nexus which, as regularly, pays back $465 to the "agent" wife, who, finally, tunnels back these refunds to her "spouse" Dr. Murphy.

And, lastly, Section 137, ss. (1), dealing with "Artificial Transactions", fits to a nicety the matter at issue: it is as follows:

> 137(1) In computing income for the purposes of this Act, no deduction may be made in respect of a disbursement or expense made or incurred in respect of a transaction or operation that, if allowed, would unduly or artificially reduce the income.

For the reasons given, this appeal is dismissed with costs in favour of the respondent.

Toronto 1968 Feb. 27-29 — Ottawa May 3

BETWEEN:

SHERRITT GORDON MINES, LIMITED .... APPELLANT;

AND

THE MINISTER OF NATIONAL REVENUE .... RESPONDENT.

Income tax—Money borrowed to finance mine—Commitment fee paid on unadvanced money—Whether part of capital cost—Capital cost allowances—Exploration and development expense—Allocation of expenses after expenditure on basis of judgment—Whether acceptable for tax purposes—Income Tax Act, s. 11(1)(a), (c), (cb), s. 83A (2) and (3).

During 1952, 1953 and 1954 appellant borrowed $24,000,000 dollars on first mortgage bonds to finance the development of a mine, power plant and refinery. In addition to payment of interest on the money so borrowed appellant was required to pay during those years a commitment fee of 1% to 1½% per annum on the unadvanced portion of the loans from January 1952. All of appellant's funds, whether from the loans or other sources, were co-mingled and payments of interest and commitment fee were not identified as to source or object until some time after completion of the project at the end of July 1954, and expenditures were then allocated to the three properties and to exploration and development on the basis of total monthly investment during the construction period. The sum of $240,567 in commitment fees was thus allocated to the capital cost of the three properties and $110,491 in commitment fees to exploration and development expense In assessing appellant for income tax for 1958 and 1959 (appellant's first profitable years after the project was completed) the Minister allowed a deduction in respect of interest allocated as described but disallowed a deduction of commitment fees.

Held, allowing the appeal (1) the commitment fees paid in respect to the three properties during the construction period were part of the capital cost of those properties within the meaning of s. 11(1)(*a*) of the *Income Tax Act* and therefore subject to capital cost allowances, and (2) the commitment fees allocated to exploration and development expense were deductible under s. 83A(2) and (3) except such portion as was attributable to the refinery.

Held also, in the circumstances of appellant's business the allocation of interest and commitment fees retroactively on the basis of judgment and appellant's records, though not completely accurate, was fair and reasonable and acceptable for income tax purposes.

M.N.R. v. Anaconda American Brass Ltd. [1956] A.C 85; *Can. Gen. Elec. Co. v. M.N.R.* [1962] S C.R. 3; *B.C. Elec. Ry Co. v M N.R.* [1958] S.C R. 133; *Chancery Lane Safe Deposit and Office Co. v. C.I.R.* (1965) 43 Tax Cas. 83; *Hinds v. Buenos*

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Ayres Grand National Tramways Co. [1906] 2 Ch. 654; *Fraser v. C.I.R.*, 25 F (2d) 653; *Georgia Cypress Co. v. South Carolina Tax Comm'n.* 22 S.E. 2d 419, considered.

INCOME TAX APPEALS.

J. F. Howard, Q.C. and *J. B. Tinker* for appellant.

D. G. H. Bowman and *Gordon Anderson* for respondent.

KERR J.:—These appeals under Part I of the *Income Tax Act* from re-assessments of the income tax of the appellant (hereinafter referred to as Sherritt) for its 1958 and 1959 taxation years were heard together in Toronto. They relate to disallowances by the Minister of National Revenue in respect of amounts that it had paid in the years 1952, 1953 and 1954 as a "commitment fee" pursuant to financing agreements with J. P. Morgan and Co. Incorporated and certain other companies, whereby Sherritt obtained $24,000,000 (United States funds) from sale of first mortgage bonds and agreed to pay, in addition to interest on the bonds, a commitment fee at the rate of 1% per annum in respect of Series A and Series B bonds and 1½% per annum in respect of Series C bonds, on the daily average unadvanced portion of the total amount that the lenders were obligated to lend under the provisions of the agreements, as set forth in paragraph 9 of the agreement dated June 13, 1952 (Exhibit 2) and paragraph 5 of the agreement dated April 12, 1954 (Exhibit 8).

Sherritt acquired a nickel-copper-cobalt property at Lynn Lake, Manitoba, in 1945 and by the end of 1951 had done considerable work in proving the ore body and in developing the mine project, which eventually included a power plant at Laurie River (about thirty-five miles from the mine) and a refinery at Fort Saskatchewan, near Edmonton, for production of metal from ore concentrates from the mine. The company planned a program of work to complete the entire project and in that work, in the years 1952, 1953 and 1954, expended the proceeds from the bonds and also money from other sources. The company made payments of bond interest and payments of commitment fee in those years, and subsequently attributed and allocated the amounts of such payments in its accounts to (a) exploration and development expenses (b) the cost of depreciable assets required and (c) operating expenses. I will refer later to the source and use of all funds and the allocation of interest and commitment fee payments.

In computing its taxable income from its 1958 and 1959 taxation years Sherritt deducted, as exploration and development expense, the portions of the bond interest and commitment fee payments in the years 1952, 1953 and 1954 that it had allocated to that expense; and claimed capital cost allowance in respect of the portions of the bond interest and commitment fee payments that it had allocated to the capital cost of depreciable assets acquired. The Minister allowed deductions claimed in respect of the payments of bond interest but disallowed the deductions claimed in respect of the payments of commitment fee.

In the Notice confirming the assessment of income tax for the 1958 and 1959 taxation years the Minister stated:

> . . . that the amount of $110,491 84 paid by the taxpayer in the taxation years 1952, 1953 and 1954 as commitment fees is not an exploration, prospecting or development expense and accordingly is not an allowable deduction under the provisions of section 83A of the Act in determining the income of the taxpayer for the 1958 and 1959 taxation years; that the amount of $240,567.19 paid by the taxpayer in the taxation years 1952, 1953 and 1954 as a commitment fee is not a part of the capital cost of the depreciable property owned by the taxpayer in the 1958 and 1959 taxation years.

In the Reply to the Notice of Appeal with respect to Sherritt's 1958 taxation year the Minister stated:

> 9. The Respondent says that of the amount of $3,163,410 70 claimed by the Appellant in the taxation year 1958 as development and exploration expenses, a portion thereof amounting to $110,491.84 represents a portion of an amount paid as commitment fees by the Appellant in the taxation years 1952, 1953 and 1954, pursuant to the agreement dated June 13th, 1952, referred to in paragraph 3 of the Notice of Appeal and is not properly deductible in computing the Appellant's income for the 1958 taxation year under section 83A of the *Income Tax Act* because the said commitment fees are not exploration, prospecting or development expenses within the meaning of section 83A of the *Income Tax Act.*
>
> 10. The Respondent says that no part of the commitment fees paid by the Appellant pursuant to the agreement dated June 13th, 1952, referred to in paragraph 3 of the Notice of Appeal, formed

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part of the capital cost to the Appellant of any property of the Appellant described in any of the Classes of Schedule B to the Regulations made pursuant to the *Income Tax Act*.

11. The Respondent says that if the commitment fees are interest on borrowed money, they were deductible under the provisions of paragraph (*c*) of subsection (1) of section 11 of the *Income Tax Act* in computing the Appellant's income for its 1952, 1953 and 1954 taxation years, and hence no portion was deductible under subsections (2) and (3) of section 83A of the *Income Tax Act* and no portion may be included in the capital cost to the Appellant of any property owned by it in the 1958 taxation year.

The Minister took a similar position in disallowing capital cost allowance claimed by Sherritt for its 1959 taxation year in respect of amounts paid as commitment fee in 1952, 1953 and 1954.

The years 1952, 1953 and 1954 are of particular significance, for they were a period of construction and development of Sherritt's Lynn Lake project, i.e., the mine at Lynn Lake, the power plant at Laurie River and the refinery at Fort Saskatchewan, in which Sherritt expended the proceeds from the bonds, and it was payments of bond interest and commitment fee "during construction" in those years that Sherritt capitalized.

It will be useful, I think, to outline the circumstances that led to the borrowing of money by Sherritt, the use of the borrowed money together with other funds of the company, the payment of bond interest and commitment fee and the allocation and treatment of the interest and commitment fee by the company, and I will endeavour to give the substance of the portions of the evidence, as I understand it, that I consider to be the more important and useful in determining the issues that are before the court for decision in these appeals.

Sherritt was incorporated in 1927 and from that time until 1951 was a relatively small mining company. It operated a copper and zinc mine at Sherridon, Manitoba, but suspended operation of that mine in September, 1951, following exhaustion of the ore body. In the years 1952, 1953 and 1954 the company's only business, other than shutting down the Sherridon mine and doing a minor amount of exploration, was its Lynn Lake project.

In 1951 the company prepared a study and a booklet setting forth plans for its Lynn Lake project, the estimated costs and the total capital expenditures involved. The estimated total costs were $42,810,000. Of that total the amount to be expended after June 30, 1951, was $32,812,000. The company planned at that time to raise $19,760,000 through sale of first mortgage bonds. This study and booklet formed the basis of discussions between Sherritt and J. P. Morgan and Co. and other lending companies, and led to the subsequent financing agreements and sale of bonds. The companies with which Sherritt entered into the financing arrangements were the Morgan Co., Bankers Trust Company, Newmont Mining Corporation, Metropolitan Life Insurance Company and other companies.

Mr. David D. Thomas, President of Sherritt, testified that the financing arrangements started in the fall of 1951 and that an oral agreement was reached that the lenders were committed to lend the agreed amount of money at 4% per annum on Series A bonds and at $4\frac{3}{4}$% on Series B bonds as of January 1, 1952, although the first written agreement (Exhibit 2) was not signed until June 13, 1952; also that payment of a commitment fee was a matter of discussion from the first time the parties talked and there was oral agreement that the commitment fee would commence on January 1, 1952. The agreement (Exhibit 2) provided for payment of the commitment fee to commence from that date. Mr. Thomas also stated that other possible sources of funds had been investigated and the company felt that they were less attractive to the shareholders than the arrangements made with Morgan and Co. and that the only way Sherritt could obtain money from the lenders was on the basis of the conditions set forth in the Mortgage Indenture that was entered into by the parties.

The first agreement provided for the authorization by Sherritt of $4,400,000 of first mortgage bonds Series A, and an issue of $17,600,000 of first mortgage bonds Series B, to be secured by a mortgage. The Mortgage Indenture, dated as of November 1, 1952, provides for payments to Sherritt by Morgan and Co., as trustee for the bond holders, from

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the money proceeds of the bonds upon certain conditions, one of which was that the money would be advanced against "bondable expenditures" certified by Sherritt as having been spent on property, plant and equipment and on deferred development of the Lynn Lake project. The definition of "bondable expenditures" on page 5 of the Mortgage Indenture (Exhibit 3) is in part as follows:

> The term "Bondable Expenditures" shall mean expenditures charged or properly chargeable to the capital accounts of the Company entitled "Property, Plant and Equipment" and "deferred Development Expenditures—Lynn Lake Project" or similar titles, in accordance with the accounting practices followed by the Company in the preparation of its balance sheet dated December 31, 1951, or charged or properly chargeable to other capital accounts of the Company in accordance with generally accepted accounting principles, made in connection with the acquisition or construction by the Company or by Laurie of property as part of the Company's Program . . .

Supplemental Indentures reduced the aggregate amount of the Series A and B bonds to $21,000,000 and added $6,000,000 Series C bonds. The procedure for taking down money upon proof of bondable expenditures was the same for the Series C bonds as for the A and B bonds. The commitment fee in respect of Series C bonds was 1½% per annum as from March 15, 1954.

Mr. W. A. Johnson, an underwriter with A. E. Ames and Company Limited, with responsibilities to advise and aid companies in securing financing, testified as an expert witness that it is general practice for institutional lenders to ask for a commitment fee on mortgage financing for a natural resource development and large construction purposes; that the majority of lenders look upon the commitment fee as additional yield on the loan, that it is paid on an amount that has not been advanced and is payable to the lender for the period from the time the lender commits to make the loan until the loan is actually made; and that the commitment fee accrues over equal periods of time like interest.

The issuance of bonds and the amounts received therefrom by Sherritt are shown in Exhibit 6 set forth next.

SHERRITT GORDON MINES LIMITED
SCHEDULE OF FIRST MORTGAGE BONDS ISSUED
YEARS 1952–1954 INCLUSIVE

	Series A	Series B	Series C	Total
Bonds issued U.S. funds				
December 23, 1952..	$ 1,000,000 00	$ 4,000,000.00		$ 5,000,000.00
June 29, 1953 .	1,400,000.00	5,600,000.00		7,000,000.00
October 30, 1953....	1,400,000.00	5,600,000.00		7,000,000.00
March 25, 1954	300,000.00	1,700,000.00		2,000,000.00
May 15, 1954 .			$ 3,000,000.00	3,000,000.00
	$ 4,100,000.00	$16,900,000.00	$ 3,000,000.00	$24,000,000.00
Money received from trustee U.S. funds				
December 26, 1952 .	$ 795,000 00	$ 3,180,000.00	$	$ 3,975,000.00
March 30, 1953 ..	205,000 00	820,000 00		1,025,000.00
June 30, 1953	1,320,000.00	5,280,000.00		6,600,000.00
October 30, 1953	1,160,000.00	4,640,000.00		5,800,000.00
December 31, 1953 .	320,000.00	1,280,000.00		1,600,000.00
March 29, 1954	300,000.00	1,700,000.00		2,000,000.00
May 17, 1954			3,000,000.00	3,000,000.00
	$ 4,100,000.00	$16,900,000.00	$ 3,000,000.00	$24,000,000.00
Proceeds from money received Canadian funds				
Bonds issued				
December 23, 1952	$ 977,061.20	$ 3,908,244.81	$	$ 4,885,306.01
June 29, 1953	1,380,724.50	5,522,897.98		6,903,622.48
October 30, 1953	1,359,922.43	5,439,689.72		6,799,612.15
March 25, 1954	294,466 87	1,668,994.74		1,963,461.61
May 15, 1954			2,951,847.55	2,951,847.55
	$ 4,012,175.00	$16,539,827.25	$ 2,951,847.55	$23,503,849.80

The money spent by Sherritt in its Lynn Lake project came partly from the proceeds from the bonds and partly from other sources. Exhibit 7, set forth next, is a statement of the source and use of funds for the period January 1, 1952, to December 31, 1954:

SHERRITT GORDON MINES LIMITED
STATEMENT OF SOURCE AND USE OF FUNDS
FOR THE PERIOD JANUARY 1, 1952 TO DECEMBER 31, 1954

	U.S. Funds	Canadian Funds	
Funds were obtained from			
Net cash profit for the years 1952–1954 inclusive			$ 2,142,859.48
First mortgage bonds issued			
Series A	$ 4,100,000.00	$ 4,012,175.00	
Series B	16,900,000.00	16,539,827.25	
Series C	3,000,000.00	2,951,847.55	
	24,000,000.00	23,503,849.80	
Less Series A due in 1955	2,343,000.00	2,292,811.23	
	21,657,000.00		21,211,038.57
Convertible debentures issued			8,000,000.00
Advances from the United States Government	4,345,671.33	4,221,731.65	
Less minimum repayment due in 1955	217,283.57	211,086.58	
	4,128,387.76		4,010,645.07
			35,364,543.12
Decrease in working capital			3,783,219.05
			$39,147,762.17

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Funds were used for		
Expenditures on property, plant & equipment		
Lynn Lake mine plant .	$ 7,168,848 37	
Laurie River power plant	1,746,324 81	
Fort Saskatchewan chemical metallurgical plant	24,045,721 11	
	32,960,894 29	
Less construction materials on hand January 1, 1952	591,481.61	32,369,412.68
Deferred development expenditures—Lynn Lake project		4,314,424.45
Housing loans advanced to employees .		329,943 79
Inventory of nickel concentrates in storage as security for advances from U.S. Government repayable after 1955		2,056,937.26
Other deferred expenditures and sundry investments		77,043.99
		39,147,762.17
Working Capital		
As at December 31, 1951		4,983,207 25
Decrease during the period		3,783,219.05
As at December 31, 1954		1,199,988 20

Exhibit 7 shows funds from all sources in the years 1952, 1953 and 1954, total capital expenditures in those years on the Lynn Lake mine plant, Laurie River power plant and Fort Saskatchewan refinery, and deferred development expenditures on the project. (There also were expenditures prior to 1952 but they are not included in the exhibit.) These deferred development expenditures were said by Mr. Thomas to be the pre-production expenses involved in bringing the mining facility into production and included the sinking of the mine shafts, underground exploration, test milling programs to find out whether the ore could be put into the form of a concentrate, metallurgical research work done in developing a refining process, housing loans advanced to employees, and general administration expenses.

Mr. Thomas said that all the money received from the bonds was used in the development of the Lynn Lake project and was applicable to the property, plant and equipment account and to deferred development expenditures. Sherritt's accounts were kept on an accrual basis of accounting which showed the total cumulative monthly investments in the property accounts, the fixed assets of the Lynn Lake project at its three locations, plus deferred development expenditures, spent or accrued from January 1, 1952, through to December 31, 1954, regardless of the source of the funds used.

Exhibit 10, next, is a statement of net interest and commitment fee expenditures in the years 1952, 1953 and 1954.

SHERRITT GORDON MINES LIMITED
SCHEDULE OF NET INTEREST EXPENDITURES
YEARS 1952-1954 INCLUSIVE

	Commitment fee	Bond interest	Interest on G.S.A. advances	Interest income	Net interest expense
1952 .	213,467 09	4,960.96		121,784.80	96,643.25
1953 .	120,474 62	439,304.81		115,508.34	444,271.09
	333,941.71	444,265.77		237,293.14	540,914.34
1954 .	48,634.35	1,068,767 98	96,717.12	26,550 21	1,187,569 24
	382,576 06	1,513,033.75	96,717.12	263,843.35	1,728,483.58
Less 1954 direct charges to operating account	18,267.73	487,174 31	96,717.12	6,758 67	595,400.49
Amount allocated	364,308 33	1,025,859 44	—	257,084 68	1,133,083.09

The interest figures in Exhibit 10 include interest paid on certain advances received by Sherritt from General Services Administration, a Department of the United States Government. Interest income in the exhibit is interest earned by Sherritt from the investment of surplus funds, including interest from short term investment and money received from Morgan and Co. The exhibit does not show what interest income was from investment of money received from Morgan as opposed to interest on other money.

The net interest (including commitment fee) expenditures in Exhibit 10 amount to $1,728,483.58. During the entire period from January 1, 1952, to December 31, 1954, net interest was allocated by Sherritt to deferred development expenditures. Then, in January 1955, by which time the accounts for the three years were said to be finalized, the company allocated the net interest amount to the individual property, plant and equipment accounts for the Lynn Lake mine, the Laurie River power plant and the Fort Saskatchewan refinery, and also allocated a portion to deferred development expenditures. The allocation was made to the various capital asset accounts on the basis of total monthly investment in the fixed assets accounts during those years, excluding investment prior to January

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1952. The company made no distinction between interest and commitment fee in this allocation, the amount allocated being the net aggregate amount of interest and commitment fee.

Exhibit 11, set forth next, shows the distribution of interest and commitment fee made by Sherritt in January 1955, and the interest as distributed by type.

(NOTE. This is the left half of Exhibit 11)

Sherritt Gordon Mines Limited
Summary—Net Interest Expense Distribution
Years 1952–1954 inclusive

	Total 1952–1954	Interest distributed by year 1952	1953	1954
Property, plant and equipment				
(a) Lynn Lake	153,358.72	27,323.39	114,985.93	11,049.40
(b) Laurie River power plant .	19,893.88	18,460.60		1,433 28
(c) Fort Saskatchewan chemical metallurgical plant . .	585,472.53	16,164.28	211,656 56	357,651.69
	758,725.13	61,948.27	326,642.49	370,134.37
(d) Deferred development expenditures.	200,165.36	34,694.98	117,628.60	47,841.78
(e) Operating expense. .	174,192.60			174,192.60
(f) Total interest distributed....	1,133,083.09	96,643.25	444,271.09	592,168 75
(g) Interest charged directly to operating . .	595,400.49			595,400.49
	$1,728,483.58	$ 96,643.25	$ 444,271.09	$1,187,569.24

(NOTE: This is the right half of Exhibit 11)

Interest distributed by type

	Commitment fee	Bond interest	Interest on G.S.A. advances	Interest income (credit) 1953–54 capitalized for tax purposes	1952 to income for tax purposes	Total 1952–54 excluding 1952 interest income
(a)	91,985.97	126,073.37		30,269.11	34,431.51	187,790.23
(b)	40,834.76	2,370.63		48.42	23,263.09	43,156.97
(c)	107,746.46	565,208.74		67,113.28	20,369.39	605,841.92
	240,567.19	693,652.74		97,430.81	78,063.99	836,789.12
(d)	110,491.84	165,593.58		32,199.25	43,720.81	243,886.17
(e)	13,249.30	166,613.12		5,669.82		174,192.60
(f)	364,308.33	1,025,859.44		135,299.88	121,784.80	1,254,867.89
(g)	18,267.73	487,174.31	96,717.12	6,758.67		595,400.49
	$382,576.06	$1,513,033.75	$96,717.12	$142,058.55	$121,784.80	$1,850,268.38

The top half of the exhibit shows the total interest, including commitment fee, and its distribution by year to property, plant and equipment, deferred development and operating expense. Mr. Thomas explained that in the case of the Laurie River power plant, for example, it was completed in September 1952, and the net interest, including commitment fee, was attributed to the cumulative monthly investment, i.e., to the capital cost of the plant to that date, but that from the end of September 1952, to the end of 1953 the plant was used to supply operating or development power to the mine and therefore the interest attributable to the power plant was charged against deferred development expense at the mine as a cost of development power, and when at the end of 1953 the mine began to produce concentrate the interest was thereafter charged to operating account.

In the case of the mine, all the interest, including commitment fee, attributable to it was capitalized and until the end of 1953 was charged against property, plant and equipment or to deferred development expense, but at the end of 1953 the mine was operating and thereafter the interest attributable to that asset was charged against operating.

In the case of the refinery, interest was charged against it until it was completed and ready for operation at the end of July 1954, and thereafter was charged against the operations of the company.

The refinery was ready for operation, as stated, at the end of July 1954, and after that date all the interest was charged against the operations of the company.

The bottom half of Exhibit 11 shows the interest and commitment fee distribution by type. This analysis was not made until 1958, following a communication from the Department of National Revenue that payments of commitment fee would not be allowed as a taxable expense for income tax purposes. At that time the company broke down the interest expense in the years 1952, 1953 and 1954 into commitment fee, bond interest, interest on G.S.A. advances and interest earned, and separated them between its

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Lynn Lake plant, Laurie River plant, Fort Saskatchewan plant, deferred development expense and operating expense. The result was an attribution of commitment fee as follows: $240,567.19 to property, plant and equipment at the three locations; $110,491.84 to deferred development expenditures; and $31,517.03 to operating expense. (It was the deductions claimed by Sherritt in respect of the first two amounts that the Minister disallowed).

Mr. Thomson gave evidence to the effect that Sherritt's funds from all sources were co-mingled in the company's bank account or accounts and no record was kept as the money was being spent as to the particular source of the money; when a payment of interest or commitment fee was made it was not at that time allocated to or identified with any particular project or particular asset; the company decided to charge all interest and commitment fee to deferred development as a suspense account until the construction period was completed and would then make an allocation project by project or asset by asset; the allocation made in January 1955, was for accounting purposes. but later there was a greater breakdown by classes of assets; the allocation was not made on the basis of tracing a particular asset expenditure to a particular source of money, and in allocating the bond interest and commitment fee no differentiation was made between them.

Exhibit 15 shows the company's allocation to capital cost classes for income tax purposes of the net interest expense that was capitalized in the years 1952, 1953 and 1954. In the case of Lynn Lake and Laurie River the expense was totally allocated to Class 10, the only tax class; at Fort Saskatchewan it was allocated to the appropriate tax class on the basis of the final construction value at the end of 1954. The commitment fee was allocated in the same proportion as the interest, and the allocation was based upon the total money invested from the funds of the company from all sources.

Mr. Thomson also indicated that although the attribution of interest to property and to deferred development expense was made in January 1955, an issue with the

Department of National Revenue did not arise in respect of it until 1958, because in the years 1952 to 1957, inclusive, Sherritt had nil income tax assessments, and it was not until 1958 that the company had an assessment from which it could make an appeal.

Two chartered accountants, Mr. John R. Barker and Mr. Stephen Elliott, were called by counsel for Sherritt as experts in accounting. Mr. Barker expressed his opinion that Sherritt's treatment of payments of commitment fee and the company's capitalization and allocation of the payments of interest and commitment fee between depreciable assets and development expense was in accordance with generally accepted accounting principles and practice. He said that it is generally accepted accounting practice to add commitment fee and interest expended during a construction period to the cost of the construction, and that in a mining enterprise a similar treatment would be appropriate in the case of development expenses. He also said that to undertake a capital construction of the magnitude that Sherritt did, requires the bringing together of three factors, labour, materials and capital; capital had to be raised to complete the construction, and the interest and commitment fee incurred during the construction period is just as real a cost of that construction as the bricks and mortar; and capitalizing or adding the interest and commitment fee to the cost of construction establishes a base for depreciation in which the total capital cost is charged to the operations of the company over the useful life of the plant, thereby bringing about a proper matching of expenses with revenues during the operating life of the company; also that if interest during construction is not capitalized it must be charged to operations and thereby create a loss during construction, with the result that the company is operating at a loss before it has begun active operation, which not only does not represent proper matching of the total cost of the project over its useful life, i.e., the adequate matching of costs with revenues, because the period during which the money is expended does not coincide with the periods during which the benefit of that expense is going to be

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realized, but is also unfair to present shareholders in that for them there would be an expense and a loss whereas for future shareholders there would be a benefit because they would not have to bear that expense.

Mr. Barker also agreed that there are a number of factors and variables to be considered in deciding whether or not to capitalize interest during construction and these factors include income from other operations of a company, the significance and size of the interest expense, the co-mingling of funds and their segregation, the source of the funds and the purpose for which they are used, and the length of the period of construction. He agreed also that there is some difference of opinion as to whether interest during construction should be capitalized and there is also a view held that interest is a money cost or a financing cost and should either not be capitalized at all or, if capitalized, should not be charged to a particular asset but to an intangible account and written off over a period of time; also that it is difficult to find anything specific on commitment fee as such, and his opinion in respect of such fee expense is related to his experience with interest and other types of expense incidental to a particular project construction.

In Mr. Barker's opinion it would have been improper for Sherritt to isolate the interest during construction, take it out of development expenses and charge it as an operating loss.

Mr. Elliott gave his opinion that interest paid during the construction period with respect to funds borrowed for construction, and commitment fees paid for the availability of those funds, are properly capitalizable as part of the cost of the particular project for which the funds were expended; that it is accepted and proper accounting to attribute this expense to the cost of physical assets constructed; and that the commitment fee is paid only so long as the funds are not borrowed, only so long as the project is incomplete, and it is inherently a part of the cost of construction. He said that the generally accepted accounting principle, described as matching costs with revenue, is that in order to measure the income of a period the revenue of the period should be charged with the costs applicable to that period; if the cost of a service that will be derived from a capital asset in the future is charged off against income during a current period the income of the current period would be under-stated and, conversely, the income of the future period would be overstated by reason of the fact that there would be no charge against the revenue of the future period for the costs of the service rendered by that capital asset in that future period; and that a determinative factor in deciding at what time the capitalization of interest should cease is that the property be in a condition to be utilized to earn revenue.

Mr. Elliott also gave his opinion that in Sherritt's case the funds were borrowed for the Lynn Lake project and the interest and commitment fee paid during the construction period were properly attributable to that project and were part of the cost or expense of the development work or the depreciable assets and should be attributed to these accounts; the commitment fee should as a matter of principle be allocated along with the interest and proportionately thereto and that it is fair and reasonable to allocate the interest and commitment fee to the investment in the particular projects for which the funds were borrowed.

Mr. Elliot also said that the practice of capitalizing interest during construction started with utilities but has carried over into other types of companies and is accepted and preferred accounting practice in industrial companies as well as in utilities.

Professor W. B. Coutts, a chartered accountant and Professor of Accounting at the School of Business in the University of Toronto, was called as an expert by counsel for the Minister. His opinion was that capitalization of interest during construction as part of the cost of the assets acquired is not preferable treatment, because it involves too great a departure from the usual accounting basis of valuing or attaching a dollar figure to fixed assets in the accounts, which normally is restricted to costs directly related to the assets; interest is usually regarded as a financing cost, part of the cost of capital treated as a cost in the

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period in which it is incurred; the capitalization of interest during construction leads to inconsistencies within and between companies, such as the fact that an asset acquired by borrowing will show a different cost from the cost of an asset acquired out of equity funds, and the fact that an asset acquired at a time when the company is not engaged in other activities might be capitalized more readily than in the case of a company engaged in other activities; and when interest is capitalized it produces a cost figure that is not really consistent or in conformity with the usual way of valuing fixed assets. As to commitment fees, his opinion was that they are even less justifiably included in the capital asset costs than interest is—such fees seem to be a cost of not using capital in the asset and it is difficult to find any logical relationship between the amount of the commitment fee and the amount of any subsequent investment in fixed assets. As to the allocation of commitment fee expenses to particular assets, he could see no direct relationship between the fee and the amount invested in the asset at a particular time. Counsel for Sherritt showed Professor Coutts excerpts from balance sheets of a number of companies (Exhibit 15) which indicate that interest during construction has been capitalized. Professor Coutts agreed that the practice is more prevalent now than it was ten years ago and also that since 1956 his work has been in the academic world and since that year he has not had any close connection with actual practice.

The three accounting experts were questioned at some length in exploration of their opinion and Professor Coutts commented on extracts from books on accounting to which his attention was drawn by counsel for Sherritt.

The evidence satisfies me that Sherritt found it necessary to borrow, and did borrow, through the bond financing described in the evidence, money that it needed to complete its Lynn Lake project, which consisted of its Lynn Lake mine, Laurie River power plant, Fort Saskatchewan refinery and related facilities, all of which were inter-related with the objective of mining ore from the mine and converting it into concentrates from which saleable metals would be produced; that the money was borrowed exclusively for that project and was expended on it in the years 1952, 1953 and 1954, that payment of the commitment fee, in addition to interest on the bonds, was a requirement of the borrowing and a condition upon which the money was lent; and that the payments of bond interest and commitment fee were made and allocated as reported by Sherritt.

In the Notice of Appeal Sherritt suggested that the commitment fee is interest on borrowed money within the meaning of section 11(1)(*c*) of the *Income Tax Act*. That suggestion was not made at the hearing by counsel for Sherritt, who put Sherritt's case on other grounds. My conclusion is that the commitment fee is not interest.

The submission of counsel for Sherritt was substantially as follows:

1. In the absence of definition in the *Income Tax Act* of "expense" or "cost", these words are to be construed in their normal and ordinary meaning in accordance with accepted commercial principles and practice.

2. It is a fundamental principle of income tax law that expenditures are required to be attributed to an appropriate period in order to compute accurately the income of each period.

3. So-called financial costs, including interest and commitment fee, expended in a construction period are, in accordance with generally accepted accounting principles and practice, properly attributed to the capital cost of the fixed assets constructed, where the borrowing was done for the purpose of the construction; this treatment is based on the necessity to defer such costs over the useful life of the assets in order to give a fair and accurate statement of the income of the taxpayer in each of the periods in which the assets are used to produce revenue.

4. The amounts of commitment fee attributed and allocated by Sherritt in respect of the construction period to the capital cost of depreciable assets are part of the capital cost of those assets within the meaning of section 11(1)(*a*) of the Act and Regulations.

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5. The amounts of commitment fee attributed and allocated by Sherritt to exploration and development expenses are prospecting, exploration and development expenses incurred by Sherritt in searching for minerals in Canada in the years 1952, 1953 and 1954 within the meaning of section 83A(2) and (3) of the Act.

6. The payment of commitment fee is, from the point of view of problems raised by this case, of the same character as a payment of interest and there is no ground for treating commitment fee expense differently from interest expense during the construction period.

7. The method of allocation of the commitment fee followed by Sherritt on the basis of the *pro rata* amount of capital investment in the assets is approved by accounting practice and is fair and reasonable.

8. Sections 11(1)(*a*) and 83A and Regulation 1100 permit the deductions claimed by Sherritt.

The main points of argument submitted by counsel for the Minister were as follows:

1. Sherritt has not established as a fact that the commitment fees are part of the capital cost to it of the assets to which it seeks to attribute them or that they are prospecting, exploration and development expenses in searching for minerals within the meaning of section 83A of the Act.

2. Neither interest nor commitment fees may, as a matter of law, be treated under the Act as part of the capital cost of assets or prospecting, exploration and development expenses within the meaning of section 83A.

3. Interest and commitment fees are costs related to the raising of capital but not a cost of the assets acquired. Commitment fees may perhaps now be deducted, in the year in which they are incurred, under section 11(1)(*cb*) which covers general expenses in connection with raising capital, but that section was not enacted until 1955 and was not in force or applicable to the years 1952, 1953 and 1954 in which the fees were paid. The deduction in those years of commitment fees was prohibited by section

12(1)(*b*) and they cannot be deducted through the indirect route of sections 11(1)(*a*) and 83A. If interest and commitment fees can be capitalized as part of the capital cost of assets and deducted under section 11(1)(*a*), then sections 11(1)(*c*) and 11(1)(*cb*) are superfluous.

4. The legally incorrect result of capitalizing interest on borrowed capital is that it is deducted indirectly through the capital cost allowance route of section 11(1)(*a*) or the route of section 83A; there is only one way of deducting interest and that is under section 11(1)(*c*) in the year in which it is paid or incurred.

5. Capital cost to a taxpayer of depreciable property is the price he pays for it, not the price he pays to obtain the funds; it is plain from an examination of section 20 of the Act that the Act does not contemplate inclusion of interest in the capital cost to the taxpayer.

6. Capitalizing interest during construction is not consistent with the scheme of Part XI of the Regulations, which sets out generally rules for deducting capital cost allowance.

7. The scheme of section 83A is inconsistent with the theory that costs related to the raising of capital should be treated as exploration and development expense.

8. The capitalization of interest paid or accrued during a construction period depends on a large number of variables, is illogical and inconsistent, results in unfairness as between taxpayers, and should be rejected as a sound basis for determining capital cost or exploration and development expenses. There is no legal or logical basis for treating interest incurred during a construction period as part of the capital cost of assets, and treating interest subsequent to the construction period as a current deduction.

9. Sherritt's monies from all sources went into a comingled fund and were paid out without identification as to source.

10. The unadvanced amounts in respect of which the commitment fee was paid were not earmarked or segregated for any particular purpose.

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11. When a payment of commitment fee was made, it was not identified with any particular asset or activity.

12. The percentage allocation made by Sherritt was notional, retroactive and hypothetical and based on total cumulative monthly investment from all sources and not on any particular attribution to source.

13. The allocation of commitment fee follows the allocation of interest, i.e., it is in the same proportion, and does not take into account the difference between interest and commitment fee, the former being based on the amount of capital borrowed and the latter on the amount that had not been borrowed.

Counsel for Sherritt referred to the following cases in support of his argument:

Whimster & Co. v. C.I.R. 12 T.C. 813;
Russell v. Town and County Bank Ltd, 13 App. Cas. 418;
Hinds v. Buenos Ayres Grand National Tramways Co. [1906] 2 Ch. 654;
Chancery Lane Safe Deposit and Office Co. v. C.I.R., 43 T.C. 83;
Bardwell v. Sheffield Waterworks Co., L.R. 14 Eq 517;
Lions Equipment Ltd. v. M.N.R. (1964) 18 D.T.C. 35;
Dominion Taxicab Ass'n v. M.N.R. [1954] S.C.R. 82;
Robert Addie & Sons' Collieries Ltd. v. C.I.R., 8 T.C. 671.

Counsel for the Minister referred to the following cases in support of his argument:

Gunnar Mining Ltd v. M.N.R. [1966] Ex. C.R. 310; [1965] C.T.C. 387; affirmed [1968] C.T.C. 22;
Imperial Oil Ltd v. M.N.R. [1947] C.T.C. 353;
Trapp v. M.N.R. [1946] Ex. C.R. 245; [1946] C.T.C. 30;
M.N.R. v. Anaconda American Brass Ltd [1956] A.C. 85;
Montreal Coke & Mfg Co. v. M.N.R. [1941] Ex. C.R. 21; [1942] S.C.R. 89; [1944] A.C. 126; [1942] C.T.C. 1; (affirmed) [1944] C.T.C. 94 (P.C.);
Madden v. Nelson and Fort Sheppard Ry Co. [1899] A.C. 626;
re Farm Security Act [1947] S.C.R. 394;
Riches v. Westminster Bank Ltd [1947] A.C. 390;
Halsbury, 3rd ed., vol. 27, p. 7;
A. G. Ont. v. Barfried Enterprises Ltd [1963] S C.R. 570; 42 D.L.R. (2d) 137;
Canada Safeway Ltd v. M.N.R. [1956] Ex. C.R. 209; [1957] S.C.R. 717; [1957] C.T.C. 335;
Cree Enterprises Ltd v. M.N.R. [1966] C.T.C. 166; 16 DTC 5158;
City of Birmingham v. Barnes [1935] A.C. 292;
Fraser v. C.I.R. (Circuit Court of Appeals, Second Circuit) 25 F. (2d) 653;
Hays v. Gauley Mountain Coal Co. 247 U.S. 189;
Georgia Cypress Co. v. South Carolina Tax Comm'n., 22 S.E. 2d 419.

The question of deductions claimed by Sherritt and allowed by the Minister in respect of bond interest payments during the construction period is not directly in issue for determination in these appeals, but Sherritt's claim for deduction of commitment fee payments during the construction period is based on the theory that inclusion of payments of interest during construction as part of the cost of the property acquired with the borrowed money is in accordance with generally accepted business and commercial principles and that such interest in Sherritt's case may be deducted under section 11(1)(*a*) as part of the capital cost to the taxpayer of depreciable property and under section 83A(2) and (3) as exploration and development expenses incurred by the taxpayer in searching for minerals in Canada. Consequently that theory must be considered.

However, even if it is found as a fact, as counsel for Sherritt submits it should be, that Sherritt's treatment of payments of bond interest and commitment fee during construction was in accordance with generally accepted accountancy principles and that the method followed was an appropriate method of accounting for Sherritt, that is not conclusive of the question the court has to decide, for the prescriptions of the *Income Tax Act* prevail.

The deductions that are permitted or prohibited, as the case may be, in sections 11, 12 and 83A are certain deductions made in computing income. The word income is defined in section 4 of the Act as follows:

> 4. Subject to the other provisions of this Part, income for a taxation year from a business or property is the profit therefrom for the year.

This leads to consideration of what is meant by profit for the year.

In *M.N.R. v. Anaconda American Brass Ltd.*[1] the Privy Council said at pages 100 and 101:

> . . . The income tax law of Canada, as of the United Kingdom, is built upon the foundations described by Lord Clyde in *Whimster & Co. v. Inland Revenue Commissioners* ((1925) 12 T.C. 813, 823) in a passage cited by the Chief Justice which may be here repeated. "In the first place, the profits of any particular year or accounting period

[1] [1956] A.C. 85.

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must be taken to consist of the difference between the receipts from the trade or business *during such year or accounting period* and the expenditure laid out to earn *those receipts*. In the second place, the account of profit and loss to be made up for the purpose of *ascertaining that difference* must be framed consistently with the ordinary principles of commercial accounting, so far as applicable, and in conformity with the rules of the *Income Tax Act,* or of that Act as modified by the provisions and schedules of the Acts regulating Excess Profits Duty, as the case may be. For example, the ordinary principles of commercial accounting require that in the profit and loss account of a merchant's or manufacturer's business the values of the stock-in-trade at the beginning and at the end of the period covered by the account should be entered at cost or market price, whichever is the lower; although there is nothing about this in the taxing statutes." . . .

In *Can. Gen. Elec. Co. v. M.N.R.*[2] Martland J. said at page 12:

In considering the validity of this conclusion, reference may first be made to some general principles which have been stated regarding the meaning of the word "profit" and the method of its determination.

Viscount Maugham, In *Lowry (Inspector of Taxes)* v. *Cons. African Selection Trust, Ltd.* ([1940] A.C. 648 at 661, 2 All E.R. 545) said:

"It is well settled that profits and gains must be ascertained on ordinary commercial principles, and this fact must not be forgotten."

In this Court, in *Dom. Taxicab Ass'n v. M.N.R.* ([1954] S.C.R. 82 at 85, 54 DTC 1020) Cartwright J. said:

"The expression 'profit' is not defined in the *Act*. It has not a technical meaning and whether or not the sum in question constitutes profit must be determined on ordinary commercial principles unless the provisions of the *Income Tax Act* require a departure from such principles."

In *B.C. Elec. Ry. Co. v. M.N.R.*[3] Abbott J. said at page 137:

Since the main purpose of every business undertaking is presumably to make a profit, any expenditure made "for the purpose of gaining or producing income" comes within the terms of s. 12(1)(*a*) whether it be classified as an income expense or as a capital outlay.

Once it is determined that a particular expenditure is one made for the purpose of gaining or producing income, in order to compute income tax liability it must next be ascertained whether such disbursement is an income expense or a capital outlay. The principle underlying such a distinction is, of course, that since for tax purposes income

[2] [1962] S.C.R. 3. [3] [1958] S.C.R. 133.

> is determined on an annual basis, an income expense is one incurred to earn the income of the particular year in which it is made and should be allowed as a deduction from gross income in that year. Most capital outlays on the other hand may be amortized or written off over a period of years depending upon whether or not the asset in respect of which the outlay is made is one coming within the capital cost allowance regulations made under s. 11(1)(*a*) of *The Income Tax Act.*

I am satisfied that at least where the amount is significant in relation to the business of a company, it is in accordance with generally accepted business and commercial principles to charge, as a cost of construction, payments of interest in respect of the construction period on borrowed money expended by the company for such construction and to write such payments off over a period of years. The practice of doing so is not as common outside the public utility field as within that field but it has extended to companies outside that field.

Having reached this conclusion, it is necessary to ask whether interest expense of this character may be deducted for income tax purposes in those years in which it is written off. I think there is no doubt that the interest is a capital outlay, the deduction of which in computing income for a taxation year, is prohibited by section 12(1)(*b*) unless its deduction is expressly permitted by some other provision of the Act. Sherritt's case is put on the basis that sections 11(1)(*a*) and 83A(2) and (3) permit deductions of amounts in the computation of which interest is a factor.

This leads to consideration, firstly, whether such interest is part of the cost of the assets acquired by the taxpayer with borrowed capital and, secondly, whether it is part of a capital cost within section 11(1)(*a*). Counsel for Sherritt cited a decision of the House of Lords in 1965, *Chancery Lane Safe Deposit and Offices Co. v. C.I.R.*[4], from which the following extracts are quoted:

> Lord Pearson, pp. 128 and 129:
>
> My Lords, the Appellant Company carries on in the basement of its buildings in Chancery Lane a safe deposit business, and lets the upper parts of the building to tenants. Most of the upper parts

[4] 43 T.C. 83.

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were destroyed by enemy action in the years 1940 and 1941. Building operations for rebuilding the upper parts and effecting some new construction were carried out in the period from 1949 to 1958. For the purpose of financing the building operations the Company borrowed large sums on mortgage in the years 1954 to 1956 and repayment was made in the years 1958 to 1961. In the meantime interest was paid on the sums outstanding and secured by the mortgages. The Company consulted its auditors as to the proper treatment of the mortgage interest in its accounts. The auditors advised the Company that, in order to give a true and fair view of the Company's affairs and in particular to bring out the cost of the building operations, and in accordance with general accountancy practice, it was proper to charge to capital the cost of finance during the period of construction in cases where the outlay was substantial in relation to the size of the Company. This was found by the Special Commissioners to be a proper method for accounting purposes, and it was adopted by the Company. A calculation was made for each of the relevant years in order to arrive at the correct proportion of the mortgage interest to be charged to capital in the Company's accounts in that year.

Lord Morris, p. 111:

In the year 1954-55 the Company paid £3,260 in mortgage interest; in the year 1955-6 the amount they paid was £11,324; in the year 1956-57 it was £26,536; in the year 1957-58 it was £29,149; in the year 1958-59 it was £28,879. In the years to which I have referred the Company decided to charge part of those sums to capital. Their decision was deliberate and calculated. It was supported by the reasoning, the soundness of which has not been challenged, that during the period of construction, when the money being spent was substantial in relation to the size of the Company, it was proper to make the cost of finance a charge to capital. The proportion of the mortgage interest which was so to be charged to capital was carefully calculated on the basis of the proportion which actual rents received bore to the estimated amount of the rents that might be obtained when the buildings were completed. By so charging to capital it was considered that a true and fair view of the Company's affairs and of the capital cost of the rebuilding and of the erection of the new buildings would be given.

Lord Upjohn, p. 119:

My Lords, when the Appellants wanted to rebuild their safe deposits premises in Chancery Lane, which had been damaged in the war, they decided to do so by financing it on borrowed money. They had, of course, to pay interest on it, and they were advised by their accountants that it would be proper to treat part of that interest as attributable to capital expenditure. That was plainly right and is not in dispute; the cost of hiring money to rebuild a house is just as much a capital cost as the cost of hiring labour to do the rebuilding. So, in their company accounts issued to shareholders for the relevant years, they debited part of the interest on the borrowed money against their profit and loss account, in the usual way, and part to capital account. This meant, of course, that the profit and loss account was not as diminished as it would have been had the whole been so debited.

Counsel for Sherritt also cited the decision of Warrington J. in *Hinds v. Buenos Ayres Grand National Tramways Co.*[5] from which I quote:

The Buenos Ayres Grand National Tramways Company, Limited, have issued certain debentures the interest on which is payable out of the profits of each year and the profits only. The question which the Court has to determine is whether the company are bound by law to charge against the profits of the year interest on money which has been borrowed expressly for the purpose of what I may call construction. It is not literally construction—it is the conversion of their horse line into an electrical traction line, but for practical purposes it is the same thing as money borrowed for the purposes of construction. The directors propose, unless they are so bound, to charge during the period of construction as part of the expenses of constructing each mile of the new line not only the money actually expended in paying for that construction, but the interest—the proportionate part of the interest—on the money which they have borrowed. Is there anything that renders it incumbent upon the company to charge that interest to the revenue account? In the first place, it is not contended that there is anything in any of the Companies Acts which in terms compels the company so to charge this interest. Neither is there any contractual stipulation to that effect in the documents which regulate the constitution of this company. The question therefore is, Is there, independently of statute, or independently of contractual stipulations affecting this company, any general rule of law which compels a company to charge interest on money borrowed for the purposes of construction against revenue, and prohibits it from charging that interest, during construction, to capital account? That really is the question which I have to decide.

In my opinion there is no such principle of law. I think the authorities establish that the principle which regulates all these questions is that which is expressed by Lord Macnaghten in the case of *Jamaica Ry. Co. v. Attorney-General of Jamaica* ([1893] A.C. 127, 136). He says in reference to expenditure, which prima facie in that particular case was income expenditure: "Nor is every item of expenditure necessarily to be debited wholly against the income of the period in which it occurs. It may be fair and proper to spread some items over a longer time." . . .

. . . In considering the accounts of a company the only principle by which the Court can be guided—of course unless there are some express words, express provisions, or express stipulations on the subject—is the consideration what a commercial man, acting fairly and honestly in the conduct of his business, would consider the proper

[5] [1906] 2 Ch. 654.

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thing to do. Now, I think that that is illustrated also by that case of *Bloxam v. Metropolitan Ry. Co.* (L.R. 3 Ch. 337). In that case the question which I have to determine directly arose. Wood V.-C. thought that the interest on borrowed money ought clearly to be charged against revenue; but the matter came before the Appeal Court, and Lord Chelmsford L.C. expressed the gravest doubt without expressly dissenting as to whether there was any such stringent rule as the Vice-Chancellor had thought. It is impossible to read the judgment of Lord Chelmsford without seeing (although he carefully guarded himself against expressly dissenting) what his views were. In a subsequent case, *Bardwell v. Sheffield Waterworks Co.* (L R. 14 Eq. 517), Malins V.-C. allowed the interest on money borrowed for the purpose of capital expenditure during construction to be added to the amount expended and to be treated as a capital charge. That is how the authorities stand. Now, what is it that the company are really proposing to do? They are creating a capital asset by means of which they will hereafter earn, or they hope to earn, profits for the company. They are not simply employing contractors to find the money and do the work. They are finding the money themselves, and they find the money by borrowing it. What does each mile of line cost them under these circumstances—what is it that they expend in constructing each mile of line, taking the amount of the borrowed money expended on that line to be £10,000., that being the company's estimate? The money is borrowed for that particular purpose—the £10,000. They have to pay interest on that £10,000. during the period that construction is taking place. In my opinion that asset which they are so constructing costs them not only the £10,000., but the £10,000. plus the amount of interest during that period of construction; and that is what they are out of pocket during the construction of that mile of line. Now, it seems to me that the company are entitled—I do not say that they are bound to do it—if they think fit to charge in their accounts as the cost of that mile of line not only the £10,000., but the £10,000. and the interest on it during the period of construction.

Counsel for the Minister cited several decisions of courts in the United States to the effect that the cost of property is the price paid for it at the time of its acquisition and that interest upon the sum invested or borrowed is not part of such cost.

Fraser v. C.I.R.[6]. On the question whether interest on borrowed money could be treated as part of the cost of real property for the purposes of income tax the court said at p. 655:

Again, at least as to interest charges, we should have to include not only that actually paid upon borrowed money, but that calculated upon the amount invested. Otherwise the profit of a speculator would

[6] 25 F. (2d) 653.

be less than that of an investor, a result contrary to common understanding. Certainly it can make no difference how the owner procures the purchase price, whether from funds in hand, or on his bare credit, or on security, or with the help of sureties. Hays v. Gauley Mountain Co., 247 U.S. 189, 38 S. Ct. 470, 62 L. Ed. 1061, decided that interest upon the amount invested was not part of the cost, and the principle there settled seems to us to involve interest on borrowed money as well.

Georgia Cypress Co. v. South Carolina Tax Commission[7] at page 422:

> In construing the word "cost" as employed in the Statute, this Court has said: "It distinctly provides that the basis of taxation and allowances for depreciation shall be the cost (not the value) of the property and additions. Now in the nature of things the cost of the property is the price paid for it at the time of its acquisition and the cost of any improvements and betterments at the time they were made." . . .

There are differing views as to whether interest during construction is part of the cost of assets acquired or constructed with the borrowed money. However, as stated, it is necessary to go further and consider whether such interest is part of the capital cost to the taxpayer of property within the meaning of section 11(1)(*a*). The subsection is as follows:

> 11. (1) Notwithstanding paragraphs (*a*), (*b*) and (*h*) of subsection (1) of section 12, the following amounts may be deducted in computing the income of a taxpayer for a taxation year:
>
> (*a*) such part of the capital cost to the taxpayer of property, or such amount in respect of the capital cost to the taxpayer of property, if any, as is allowed by regulation;

There is no decision binding on this court on that question, so far as I am aware. In my view the question is fairly arguable, but I am disposed to think that interest during construction can be a part of the capital cost of property within section 11(1)(*a*) and that in Sherritt's case a portion of the payments of bond interest and commitment fee during construction was part of the capital cost to Sherritt of the depreciable property upon which the bond money was expended, within the meaning of that subsection. The commitment fee payments were necessarily made to obtain the bond money and were payments on

[7] 22 S.E. 2d 419.

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account of capital and, although there are differences between bond interest and commitment fee, I see no persuasive reason why Sherritt's payments of commitment fee during construction should not be treated as part of the capital cost of the property if the payments of bond interest during construction are to be so treated.

In the absence of any definition in the statute of the expression "capital cost to the taxpayer of property" and in the absence of any authoritative interpretation of those words as used in section 11(1)(*a*), insofar as they are being considered with reference to the acquisition of capital assets, I am of opinion that they should be interpreted as including outlays of the taxpayer as a business man that were the direct result of the method he adopted to acquire the assets. In the case of the purchase of an asset, this would certainly include the price paid for the asset. It would probably include the legal costs directly related to its acquisition. It might well include, I do not express any opinion on the matter, the cost of moving the asset to the place where it is to be used in the business. When, instead of buying property to be used in the business, the taxpayer has done what is necessary to create it, the capital cost to him of the property clearly includes all monies paid out for the site and to architects, engineers and contractors. It seems equally clear that it includes the cost to him during the construction period of borrowing the capital required for creating the property, whether the cost is called interest or commitment fee. Such cost is a capital cost that could not be deducted as an operating expense, without special authority. Possibly as good a way as any of testing the matter is to consider the possibility of a third person creating the required assets to the taxpayer's specifications to sell them to him when completed. All their financing costs would enter into the price that the taxpayer would have to pay for the assets and there would be no doubt that the price would be the capital cost of the property to him if he bought it ready to use. If that be so, why should those costs be classified otherwise when he creates the asset himself?

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The inclusion of interest during construction as part of the capital cost of property within the meaning and for the purposes of section 11(1)(*a*) may present problems in some instances, but I do not think that an interpretation that includes such interest is inconsistent with the scheme of the Act or its capital cost allowance provisions. On the contrary, that treatment of interest during construction should, I think, help to accurately reflect the result of each taxation year's operations and the profit therefrom for that year for both business and income tax purposes, without unduly interfering with the smooth working of the Act.

Next there is the contention that section 11(1)(*c*), governing the deduction of interest, is a specific provision and that it permits deduction of interest only as a current expense in the year in which it is incurred or paid, and that a taxpayer has no option to deduct interest through section 11(1)(*a*). Section 11(1)(*c*) is as follows:

> 11. (1) Notwithstanding paragraphs (*a*), (*b*) and (*h*) of subsection (1) of section 12, the following amounts may be deducted in computing the income of a taxpayer for a taxation year:
>
> . . .
>
> (*c*) an amount paid in the year or payable in respect of the year (depending upon the method regularly followed by the taxpayer in computing his income), pursuant to a legal obligation to pay interest on
>
> (i) borrowed money used for the purpose of earning income from a business or property (other than borrowed money used to acquire property the income from which would be exempt), or
>
> (ii) an amount payable for property acquired for the purpose of gaining or producing income therefrom or for the purpose of gaining or producing income from a business (other than property the income from which would be exempt),
>
> or a reasonable amount in respect thereof, whichever is the lesser;

There is also the argument that if deduction of payments of commitment fee is permissible it is by virtue of section 11(1)(*cb*), which was not enacted until 1955 and is not applicable to the years 1952, 1953 and 1954 in which the payments here under consideration were made, and this

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subsection permits deduction of expenses only in the year in which they are incurred. Section 11(1)(*cb*) is as follows:

> 11. (1) Notwithstanding paragraphs (*a*), (*b*) and (*h*) of subsection (1) of section 12, the following amounts may be deducted in computing the income of a taxpayer for a taxation year:
>
> . . .
>
> (*cb*) an expense incurred in the year,
>
> (i) in the course of issuing or selling shares of the capital stock of the taxpayer, or
>
> (ii) in the course of borrowing money used by the taxpayer for the purpose of earning income from a business or property (other than money used by the taxpayer for the purpose of acquiring property the income from which would be exempt),
>
> but not including any amount in respect of
>
> (iii) a commission or bonus paid or payable to a person to whom the shares were issued or sold or from whom the money was borrowed, or for or on account of services rendered by a person as a salesman, agent or dealer in securities in the course of issuing or selling the shares or borrowing the money, or
>
> (iv) an amount paid or payable as or on account of the principal amount of the indebtedness incurred in the course of borrowiing the money, or as or on account of interest:

Apart from section 11(1)(*a*), (*c*) and (*cb*), interest on borrowed capital and the expenses covered by paragraph (*cb*) would not be deductible, because they are expenses in relation to capital and are not operating expenses.

As regards interest paid in a year or payable in respect of a year while the company was carrying on its business, section 11(1)(*c*) provides for its deduction in computing its income of that year. Similarly, insofar as an expense within section 11(1)(*cb*) is concerned, if it was incurred in a year while the company was carrying on its business, section 11(1)(*cb*) applies to permit its deduction in computing its income of that year.

Neither section 11(1)(*c*) nor section 11(1)(*cb*) has any application to interest, or to expenses covered by paragraph (*cb*), incurred in respect of a year in which the company is building its plant and before it starts to carry on its business. It cannot have a computation of income from a nonexistent business. (Note Section 11(1)(*c*)(i): "borrowed money used for the purpose of earning income from a business").

Section 11(1)(*a*) was designed to allow capital costs to be written off as such and clearly applies—as paragraphs (*c*) and (*cb*) do not—to the costs of a capital nature incurred before the business was commenced. There is, therefore, nothing inconsistent between applying paragraphs (*c*) and (*cb*) to expenses incurred during the operation of a business and allowing such costs incurred before the starting of the business as capital costs under section 11(1)(*a*).

I would apply the same reasoning, although it is a little more difficult, to a case where, while one business is being carried on, a substantially different one is being readied for launching.

Heretofore I have dealt with the general question whether interest during construction is deductible under section 11(1)(*a*). The circumstances in Sherritt's case add complexities to the problem. Its funds from all sources were co-mingled and were paid out without identification as to source, and when a payment of bond interest or commitment fee was made it was not identified with any particular asset or activity. It was argued by counsel for the Minister that for these among other reasons Sherritt has not established that a portion of the commitment fee paid by it is part of the capital cost of the particular assets to which Sherritt has attributed and allocated payment of such fee and in respect of which it claims deductions under section 11(1)(*a*). Counsel for Sherritt, on the other hand, says that the method of attribution and allocation followed by the company on the basis of the *pro rata* amounts involved was in accordance with accepted business and accountancy practice and was fair and reasonable.

Having regard to the mingling of funds and the method of Sherritt's bookkeeping, I have no doubt that Sherritt cannot establish exactly how much of the bond money was expended on the construction of a particular asset in respect of which it is claiming capital cost allowance. However, I think that it probably was impractical in a business sense

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for Sherritt to keep records showing the source of the funds and their application in the case of each item of expenditure. The President of the company said that it is an impossibility, or at least he had never heard of a normal business attempting to do it, to get moneys in from various sources and to pay them all into separate accounts and then to say out of this account we spent so much and so much. Expenditures were recorded on a monthly accrual basis and the total amount spent on each asset was known. The total amount of bond money spent on the project was known, as was the total amount spent from other funds. The amounts of bond interest and commitment fee payments were known. The dates of expenditures and of payments of interest and commitment fee were known. The attribution and allocation of bond money and of bond interest made by Sherritt was accepted by the Minister in respect of the deductions claimed by Sherritt and allowed by the Minister in connection with payments of bond interest during construction.

I think that in the circumstances of Sherritt's business it was proper for the company to make a retroactive attribution and allocation of bond interest and commitment fee payments on the basis of judgment and opinion and the records of the company, as Sherritt did, and although the fit may not be perfect the attribution and allocation so made was fair and reasonable and adequate and acceptable for income tax purposes (except, as stated later herein to such extent, if any, as bond interest or commitment fee was attributed to the refinery at Fort Saskatchewan as an exploration or development expense in searching for minerals).

There remains the matter of deductions of commitment fee payments claimed as exploration and development expenses under section 83A(2) and (3) which were disallowed by the Minister. They were claimed on the basis that a portion of the bond money was expended in exploration and development of the Lynn Lake mine in the years 1952, 1953 and 1954 and that an appropriate portion of the interest and commitment fee payments during the construction period in those years was attributable to exploration and development expenses and deductible as such under section 83A(2) and (3). As in the case of construction of depreciable assets, these expenses were paid out of a common fund from all sources and no record was kept that would show the particular source of the money used to pay a particular item of expense. An attribution and allocation was made on a *pro rata* basis (as already referred to in the case of depreciable property) and it was accepted by the Minister in allowing, as exploration and development expenses, bond interest attributed and allocated to such expenses.

The pertinent parts of section 83A(2) and (3) are:

> 83A. (2) A corporation whose principal business is mining or exploring for minerals may deduct, in computing its income under this Part for a taxation year, the lesser of
>
> (*a*) the aggregate of such of the prospecting, exploration and development expenses incurred by it in searching for minerals in Canada as were incurred during the calendar year 1952, to the extent that they were not deductible in computing income for a previous taxation year, or
>
> . . .
>
> (3) A corporation whose principal business is
>
> . . .
>
> (*b*) mining or exploring for minerals,
>
> may deduct, in computing its income under this Part for a taxation year, the lesser of
>
> (*c*) the aggregate of such of
>
> . . .
>
> (ii) the prospecting, exploration and development expenses incurred by it in searching for minerals in Canada,
>
> as were incurred after the calendar year 1952 and before the end of the taxation year, to the extent that they were not deductible in computing income for a previous taxation year, or

I think that the reasoning that in my view supports the inclusion of interest during construction as part of the capital cost of the depreciable property acquired or constructed through the expenditure of the borrowed bond money also supports the inclusion, as exploration and development expenses, of interest during the construction period on the borrowed bond money spent in exploration and development work in that period. Similarly in respect of commitment fee payments.

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It is not clear to me whether any portion of the payments of bond interest or commitment fee during the construction period was attributed and allocated to the refinery at Fort Saskatchewan as an exploration or development expense. I do not think that expenses paid in the development of that refinery can be said to be expenses in searching for minerals within the meaning of sections 83A(2) and (3).

The appeals are allowed and the assessments for the appellant's 1958 and 1959 taxation years are referred back to the respondent for re-assessment to allow deductions of the portions of the payments of commitment fee claimed by the appellant as exploration and development expenses and as capital cost allowance (which are referred to in the Notices of Appeal, particularly in paragraph 9 in each Notice), except insofar as such portions include an amount allocated by the appellant to its accounts concerning its refinery at Fort Saskatchewan as being exploration and development expenses deductible under section 83A of the *Income Tax Act*.

The respondent will pay to the appellant its costs of the appeals to be taxed.

BETWEEN:

Calgary 1968 Apr. 30

Ottawa May 15

DR. BARNARDO'S .... APPELLANT;

AND

THE MINISTER OF NATIONAL REVENUE .... } RESPONDENT.

Revenue—Estate Tax Act, R.S.C. 1958, c. 29, s. 7(1)(d)(i)—Appellant not an "organization in Canada".

In 1964, a decedent by his will directed the payment of the residue of his estate valued at $521,670.02 to the appellant "Dr. Barnardo's".

The respondent assessed a tax of $123,943.24 on this decedent's estate on the basis that this estate was not entitled to any deduction under section 7(1)(*d*)(*i*) of the *Estate Tax Act* because the appellant was not an "organization in Canada".

Held: 1. that the appellant, an incorporated association, was not such an "organization in Canada" to qualify a gift to it for a deduction under section 7(1)(*d*)(i) of the *Estate Tax Act* because (1) it did not have an office or place of business with any employees or even an attorney or an agent in Canada; and (2) it did not actually carry on in Canada any operation devoted to its particular charitable purpose "at the time ... of the death of the deceased".

2. That the appeal is dismissed without costs.

ESTATE TAX APPEAL.

D. O. Sabey for appellant.

D. G. H. Bowman for respondent.

GIBSON J.:—The decision on this appeal under the *Estate Tax Act* is dependent on whether or not the appellant on April 9, 1964 was an "organization in Canada" within the meaning of those words in section 7(1)(*d*)(i)[1] of that Act.

On April 9, 1964, David A. Oliver, merchant, Drumheller, Alberta died and by his will which was probated he directed the payment of the residue of his estate valued at $521,670.02 to the appellant "Dr. Barnardo's".

By Notice of Assessment dated April 1, 1965, the respondent assessed a tax of $123,943.24 against this estate on the

[1] 7. (1) For the purpose of computing the aggregate taxable value of the property passing on the death of a person, there may be deducted from the aggregate net value of that property computed in accordance with Division B such of the following amounts as are applicable:

. . .

(*d*) the value of any gift made by the deceased whether during his lifetime or by his will, where such gift can be established to have been absolute and indefeasible, to

(i) any organization in Canada that, at the time of the making of the gift and of the death of the deceased, was an organization constituted exclusively for charitable purposes, all or substantially all of the resources of which, if any, were devoted to charitable activities carried on or to be carried on by it or to the making of gifts to other such organizations in Canada, all or substantially all of the resources of which were so devoted, or to any donee described in subparagraph (ii), and no part of the resources of which was payable to or otherwise available for the benefit of any proprietor, member or shareholder thereof, or

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basis that this estate was not entitled to any deduction under section 7(1)(*d*)(i) of the *Estate Tax Act* for the purpose of computing the aggregate taxable value of property passing on the death of the deceased, because the appellant was not an "organization in Canada". (But it is common ground between the parties that the appellant was at the material time and is a charity, and otherwise (except for the words "organization in Canada") the gift to the appellant qualifies as a deduction under that subsection of the Act).

The meaning of the words "organization in Canada" in section 7(1)(*d*)(i) of the *Estate Tax Act* in relation to the facts of this case is the issue for decision.

Much expense, time, and otherwise unnecessary things would have been expended and done, for the purpose of this adjudication were it not for the fact that counsel for the parties reached an agreement on most facts, and reduced them to writing, which such agreement was filed as Exhibit A-1 at this trial.

All other evidence was adduced through Mr. Frederick James Potter, General Secretary of Dr. Barnardo's, England.

The Agreed Statement of Facts is as follows:

1. Dr. Barnardo's Homes: National Incorporated Association (hereinafter called "Dr. Barnardo's") was incorporated in Great Britain on April 20, 1899 under the English *Companies Act*, 1862, 25 & 26, Ch. 89, under the name of "The National Incorporated Association for the Reclamation of Destitute Waif Children, otherwise known as Dr. Barnardo's Homes". On May 25, 1906 it changed its name to Dr. Barnardo's Homes: National Incorporated Association. On December 31, 1965 it again changed its name to Dr. Barnardo's.

2. David A. Oliver died testate in the Province of Alberta on April 9, 1964 and left the residue of his estate to the Appellant. Clause 6 of his Last Will and Testament was as follows:

> "6. I direct my Executor and Trustee to pay the residue of my estate to charity, the sole beneficiary being Dr. Barnardo's Homes, 18 Stepney Causeway, London, England."

3. On assessing pursuant to the *Estate Tax Act*, the Respondent did not allow pursuant to section 7(1)(*d*) of the *Estate Tax Act* as a deduction from the aggregate net value of the property passing on the death of the deceased the value of the residue of the estate so left to the Appellant.

4. The Appellant is the successor to property passing on the death of the deceased within the meaning of sections 22 and 58(1)(r) of the *Estate Tax Act*.

5. At the time of the making of the gift to the Appellant and of the death of the deceased the Appellant was an organization constituted exclusively for charitable purposes, all or substantially all of the resources of which were devoted to charitable activities carried on by it. The Respondent specifically does not admit that the Appellant was an organization in Canada within the meaning of section 7(1)(*d*) of the *Estate Tax Act*.

6. The governing body of Dr. Barnardo's consists of a council of not more than twenty-five persons, who from themselves appoint two major committees, the Finance Committee and the Committee of Management. None of these persons on the council have at any material time been residents of Canada and all have been residents of the United Kingdom. All meetings of the council and of the committees have at all material times been held in England and have never been held in Canada.

7. At all material times there were between two and three hundred members of Dr. Barnardo's. At the date of death of the deceased no officer and no member of Dr. Barnardo's was resident in Canada.

8. At all material times Dr. Barnardo's was resident in England and its head office and central management and control was located in London, England. It has never been resident in Canada. The Canadian operations records were in Canada until 1960 when all records were moved to London, England. Prior to 1960 the London office received annual statements from the Canadian manager and from the auditors and received quarterly bank statements. The corporate books and records of Dr. Barnardo's have always been kept in London, England.

9. Prior to 1925 a portion of the activities of Dr. Barnardo's consisted in emigrating children from Great Britain to Canada as summarized in Exhibit ASF-1. A number of Homes and a Farm School were established in Canada for the reception of these children. After July 1, 1925 the activities of Dr. Barnardo's were greatly curtailed when the Government of Canada prohibited the admission to Canada of children under the age of 14 years unless accompanied by a parent. All emigration of children to Canada was stopped by 1939. Two of the Homes and the Farm School were sold by the end of the 1920's; two more were sold in 1941 and 1942 respectively and the last Home was sold in 1948.

10. Dr. Barnardo's continued to operate and maintain offices in the City of Toronto in the Province of Ontario until 1960. Since that time The Canadian Imperial Bank of Commerce which carries the account of Dr. Barnardo's has paid the pensions to Dr. Barnardo's retired staff in Canada, has received and acknowledged contributions to Dr. Barnardo's and has transmitted correspondence to London.

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11. Up until 1960 or 1961 Dr. Barnardo's had two bank accounts in Canada. One was a trust account containing a small amount of money consisting of amounts saved by Dr. Barnardo's boys and girls that had not been withdrawn by them. In 1960 the amounts in this account (totalling $131.24) were transferred to the general account of Dr. Barnardo's at the Avenue Rd. and Eglinton Branch of The Canadian Imperial Bank of Commerce. This account still exists. Except for the payment by the Bank of the specific pensions referred to in paragraph 14, at the date of death of the deceased no person in Canada had the authority to draw on the general account and authorization for any payments out of the account had to be made by letter from an authorized person at Dr. Barnardo's in London, England.

12. The last time that a separate audited report of the financial affairs of Dr. Barnardo's in Canada was done was in 1960 when an audited report for the year ended December, 1959 was done by Clarkson, Gordon & Company. Neither Clarkson, Gordon & Company nor any other accounting firm in Canada did any accounting work for Dr. Barnardo's after that date and no separate account relating to Canada was made by any person in Canada though a separate account was kept in London.

13. At the date of death of the deceased Dr. Barnardo's held securities such as shares or bonds in Canada and the share certificates were physically in the possession of The Canadian Imperial Bank of Commerce in Toronto. Shares or other securities were purchased in Canada by Dr. Barnardo's on the advice of and through brokers in London, Engand and on the direction of officers of Dr. Barnardo's in England. The moneys used to purchase such securities were obtained from funds derived from donations in Canada to Dr. Barnardo's or funds previously remitted to Canada by Dr. Barnardo's. No funds have been remitted by Dr. Barnardo's to Canada for any purpose since 1939. At no time have Dr. Barnardo's had a safety deposit box in Canada. Dr. Barnardo's has not withdrawn from Canada any of the gifts made to it in Canada and continues to hold its investments and funds in Canada.

14. Dr. Barnardo's paid pensions to two former employees in Canada in 1964. Apart from pensions no amounts were paid in Canada to any person for any purpose by Dr. Barnardo's from 1960 until the end of 1964.

15. After 1953 no public appeals to any person in Canada were made by Dr. Barnardo's either from England or from Canada.

16. In 1964 Dr. Barnardo's did no charitable work of any kind in Canada nor did it contribute any funds toward charitable work in Canada. Dr. Barnardo's continues to communicate and correspond from London with Old Boys and Girls providing assistance to them in dealings with various federal agencies including the Department of Veterans' Affairs and a number of social welfare agencies. All

these matters are handled from Dr. Barnardo's head office in London, England for purposes of economy and centralization. The various enquiries are summarized in Exhibit ASF-2.

17. From 1960 until the present the only property owned in Canada by Dr. Barnardo's consisted of the securities and bank account referred to above.

18. At the date of death of the deceased there was no person in Canada who had a power of attorney, either general or restricted, to execute any document or do anything on behalf of Dr. Barnardo's in Canada.

19. Attached as Exhibit ASF-3 are the returns of Information filed by Dr. Barnardo's with the Provincial Secretary of Ontario under *The Corporations Information Act* (Ontario) for the period 1959-1965 inclusive.

20. All persons shown as officers and directors of Dr. Barnardo's on the said returns were residents of England and not of Canada.

21. In 1960 all of the records of Dr. Barnardo's that had formerly been held in Canada were transferred to England and since that time Dr. Barnardo's had no telephone listing, no address, no office and no employees in Canada.

22. At no time has Dr. Barnardo's carried on in Canada the work of admitting children to care in homes similar to the work carried on by it in the United Kingdom.

23. Since 1950 no payments have been made in Canada by Dr. Barnardo's to any charitable organization other than payments made by Dr. Barnardo's to the Commission on Emotional and Learning Disorders in Children of $30,000 in 1966 and $20,000 in 1967.

24. The parties agree that the sole issue in this appeal is whether Dr. Barnardo's was an organization in Canada at the date of death of the deceased within the meaning of section 7(1)(*d*) of the *Estate Tax Act*.

This evidence established, among other things, the following facts:

On April 9, 1964, the appellant, a United Kingdom charity had these connections with Canada:

1. It had a relatively small bank account in a branch of the Canadian Imperial Bank of Commerce, Toronto, Ontario, and a portfolio of investments, the share and bond certificates representing which were physically in Canada, amounting to about $250,000.
2. From this said bank account, on specific directions from the executive officers of the appellant in England, it paid pensions to two former employees, a Mrs. Black and a Mr. Jenkins.

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3. Most letters to the appellant posted in Canada (making enquiries of age for example, of former Barnardo persons, which was the predominant type of letter sent to it,) were addressed to the appellant's office in London, England; but any that were not, were sent on by the said bank to that office.

4. It bought securities in Canada through Wood, Gundy, & Co., brokers, on specific instructions from time to time of the London, England, brokers of this appellant.

But also, as of April 9, 1964, the appellant:

1. Was not resident in Canada, in the sense that there was any management or control in Canada; (see *Swedish Central Railway Company, Limited v. Thompson*[2]; *Egyptian Delta Land and Investment Company, Limited v. Todd*[3]; *De Beers Consolidated Mines, Limited v. Howe*[4]);

2. Was not carrying on its business in Canada, although authorized to do so in the Province of Ontario, holding in good standing an extra-provincial license under Part IX of *The Corporations Act of Ontario*, R.S.O. 1960, c. 71, as amended, and having filed up to date returns under *The Corporations Information Act*, R.S.O. 1960, c. 72;

3. Did not own any real estate in Canada;

4. Had no office or telephone number in Canada;

5. Had no employees in Canada;

6. Had no representative or attorney or agent in Canada;

7. Did no charitable work pursuant to its powers in Canada;

8. Was not domiciled here;

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[2] [1925] A.C. 495.
[3] [1929] A.C. 1.
[4] [1906] A.C. 455.

9. Was not subject to any Canadian legislation except as to the Province of Ontario Extra-Provincial License authorizing it to do business in Canada;
10. In its formal annual reports made in England, from 1960 to 1964 made no reference to any operation carried on by it in Canada, but made reference to operations carried on by it in the United Kingdom, Australia, New Zealand, Kenya, and so forth.

In effect, by April 9, 1964, the appellant had accomplished what was its intention in 1954, as evidenced by part of a letter written on August 6, 1954 by the General Superintendent of the Appellant in London, England to Mr. G. Black, Toronto, its last agent in Canada, (died 1960), *viz.,*

> ...Council regards itself as winding up its affairs in Canada

Counsel agree that there is no test prescribed in the *Estate Tax Act,* and no jurisprudence as to the meaning of the words "organization in Canada" in section 7(1)(*d*)(i) thereof.

An "organization in Canada" to qualify a gift to it for a deduction under section 7(1)(*d*)(i) of the *Estate Tax Act* may be an unincorporated as well as an incorporated association.

It is relatively easy to determine whether or not the individuals of an unincorporated organization who carry on its charitable work are "in Canada", in a natural sense, but when it is sought to determine whether or not an incorporated organization is "in Canada" it is not as easy to determine, because in a natural sense a corporation cannot be "in Canada" or anywhere else. Some artificial test, in the case of the latter, must therefore be applied.

In applying such a test, it is a pure question of fact, to be determined upon a scrutiny of the charitable activities of such an organization at the material time "in Canada".

Adopting such an approach, I am of the view that the following are relevant criteria to be considered in such a test. Any organization is not "in Canada" for the purposes of section 7(1)(*d*)(i) of the *Estate Tax Act,* (1) unless the

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organization has in Canada an office or place of business with some or at least one employee, or failing that, an attorney or agent in Canada, and (2) unless also such organization actually carries on in Canada in some material way an operation devoted to the particular charitable purpose of the organization "at the time... of the death of the deceased".

In this case, the critical time is the date of death of the deceased, David A. Oliver, *viz.*, April 9, 1964.

Predicated on the findings of facts above recited, it is patent that the appellant on April 9, 1964 did not meet the test above stated.

It follows, therefore, that the appellant was not an:

> . . . organization in Canada that, at the time . . . of the death of the deceased, (i e. of the donor by will of the gift to the appellant) was... constituted exclusively for charitable purposes, all or substantially all of the resources of which, if any, were devoted to charitable activities carried on or to be carried on by it or to the making of gifts to other such organizations in Canada, all or substantially all of the resources of which were so devoted, ...[5]

(Underlining and words in brackets are mine.)

The appeal is therefore dismissed, but without costs.

[5] Section 7(1)(*d*)(i) of the *Estate Tax Act.*

BETWEEN:

Toronto 1968 Mar. 13-14 — Ottawa May 15

DORIS TRUCKING COMPANY LIMITED .... APPELLANT;

AND

THE MINISTER OF NATIONAL REVENUE .... RESPONDENT.

Income tax—Direction by Minister that two companies be deemed associated—Whether their separate existence for business reasons only—Onus of proof—Income Tax Act, s. 138A(2)(a) and (b).

D, who with her husband was a principal shareholder in a building supply company, sold all of her shares in that company to her husband in 1958 upon the incorporation of appellant company of which she was sole shareholder. Appellant company took over the seven employees and three delivery trucks of the building supply company and thenceforth performed all deliveries for the building supply company. Pursuant to s. 138A(2)(*a*) of the *Income Tax Act* the Minister directed that the two companies should be assessed for 1964 as associated companies on the ground that their separate existence was not solely for the purpose of carrying out their business most effectively. Appellant appealed alleging that it was incorporated (1) to employ the building supply company's staff and thus to free it from the consequences of a strike, and (2) to take title to a parcel of land (bought in 1959) as a site for the two businesses and thus to safeguard the land from the creditors of the building supply company in the event of its insolvency.

Held, dismissing the appeal, on the evidence appellant had not dispelled a doubt, which s. 138A(3)(*b*)(i) required it to do, that none of the main reasons for the separate existence of the two companies was to reduce the amount of tax otherwise payable.

C.I.R. v. Brebner [1967] 1 All E R 779, distinguished.

INCOME TAX APPEAL.

Wolfe D. Goodman and *Arnold L. Cader* for appellant.

M. A. Mogan and *J. R. London* for respondent.

DUMOULIN J.:—This is an appeal from the Minister's decision, dated July 27, 1967, affirming his previous assessment in the sum of $5,876.80 added, for taxation year 1964, to the appellant's reported income. For reasons to follow the amount at issue herein, is $4,117.63.

In appellant's recital of the facts it is said that D. & M. Builders Supply Limited was incorporated under the laws of Ontario, in October 1955, "to carry on business of merchants and dealers in and manufacturers of lumber, wood

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and building products". As could be expected D. & M. Builders Supply Ltd. (hereinafter called "D. & M.") became unionized sometime in June 1958, the Construction Workers' Division of the United Mine Workers obtaining certification as bargaining agent of D. & M's employees, numbering no more than seven.

At this stage the problem looms up and is set forth in paragraphs 3, 4, 5, 6 and 7 of the Notice of Appeal, most of which I think useful to quote *verbatim.*

> 3 The principals of D. & M (no others than Morris Rosenberg and his wife, Doris) were concerned about the problem created by the certification of the union and discussed it with their solicitors and accountants.
>
> 4. On the advice of their solicitors and accountants, the Appellant (Doris Trucking Company, Limited) was incorporated on November 19, 1958. The Appellant then hired the truck drivers (3 in number), warehousemen (3 also), and all other staff (i.e. Mrs. Doris Rosenberg and four office workers) covered by the union's certification with D. & M.

Paragraph 5 notes that collective bargaining between the union aforesaid, as agent of the newly transferred working crew of appellant, and the latter, has gone on since 1959. The evidence at trial and exhibit 7 would, nevertheless, establish the "unionization" of the Doris Trucking personnel as occurring on August 8, 1963.

However that may be, appellant proceeds to explain in paragraphs 6 and 7, respectively, that:

> 6 The incorporation of the Appellant (Doris Trucking Ltd.) and the hiring by it of the employees referred to in paragraph 4 above, allowed D. & M. to be free from union involvement, with the intention that if a strike were called by the union, such a strike would affect only the operations of the Appellant, leaving D. & M. free to hire other truckers and to continue operations uninterrupted by a strike. D. & M., being non-unionized could also continue to deal with unionized customers during a strike against such customers by making deliveries through other truckers, notwithstanding any refusal on the part of the Appellant's employees to deliver merchandise to such customers

Such is the first reason suggested for launching a second and separate company; the other ground for doing so differs entirely; it is alleged that:

> 7. In or about 1959, the Appellant purchased a fourteen acre parcel of land in the township of Trafalgar, on which the Appellant intended to erect a building for both its own use and for lease to D. & M. By reason of the fluctuations in the building supply business, it

was felt necessary to have title to the said property in the Appellant's name to safeguard the said property from the hazards of the building supply business.

To this prudent expectation, the unescapable conclusion must of needs be that expressed by Doris Trucking Co. in section 11, paragraph 1 of its Notice of Appeal:

1. The Appellant claims that the separate existence of the Appellant and D. & M. is solely for the purpose of carrying on the business of the two companies in the most effective manner and such separate existence is not to reduce the amount of taxes that would otherwise be payable by them.

At the hearing and in his very lucid written brief (an appreciation equally deserved by appellant's able counsel, for his accurate Summary of Argument), Mr. Mogan, for respondent, foregoing his party's initial direction of an association between D. & M. and Doris Trucking Co., contended that "the onus, by virtue of s.s. (3) of section 138A, is on the appellant to establish that none of the main reasons for the separate existence of the appellant and D. & M. Builders Supply Limited was to reduce the amount of tax otherwise payable under the *Income Tax Act,* R.S.C. 1952, c. 148".

The unsuitability of section 39(4) to the instant matter is accounted for at page 3 of respondent's Notes of Argument, hereunder reproduced:

From 1958 (when Doris Trucking obtained corporate status) until 1964, if Mr. and Mrs. Rosenberg were to avoid having D. & M. Building Supplies Limited associated with Doris Trucking Company Limited, it was absolutely essential that Doris Rosenberg dispose of her shares in D. & M. This is in fact what she did. She sold all of her shares in D. & M. to her husband Morris Rosenberg, and her husband did not acquire any shares in the new company, Doris Trucking. It is clear that D. & M. and Doris Trucking have never been associated within the meaning of Section 39(4) of the *Income Tax Act*

The ensuing lines come close enough to the gist of the problem: the nature of the pertinent evidence, *pro* or *con*, to be adduced; I quote:

Although we admit (writes respondent's counsel) that Section 39(4) is not applicable so as to make D. & M. and Doris Trucking associated, *the deliberate conduct of Mr. & Mrs. Rosenberg in arranging their share ownership in the two companies so as, to keep them from being associated is relevant in determining the reasons for the separate existence of Doris Trucking in 1964.*

(Emphasis not in text.)

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For greater clarity, may I be permitted to repeat, in respondent's words, the basic elements of this appeal. (*cf.* Notes of Argument, at pages 4, 5 & 6): Mr. Mogan writes that:

> The Appellant has advanced two principal reasons for the separate existence of Doris Trucking in 1964, and those reasons are as follows:
>
> (1) The drivers and yardmen of D. & M. were forming a union and it was the desire of Mr. and Mrs. Rosenberg to keep D. & M. free from union involvement. Mrs. Rosenberg stated (in her evidence at the trial) that if a union was organized for another company (i e. Doris Trucking Co) 'working for us', and if the union went on strike, D. & M. could get other trucks, drivers and yardmen and could continue to operate;
>
> (2) It was decided to acquire a 14-acre parcel of land in Trafalgar Township in 1959, and it was considered desirable to have some person other than D. & M. hold the land Mrs. Rosenberg stated that there was a certain amount of risk in the business carried on by D. & M, and that she and her husband wanted to keep this land free from any potential action by creditors in the event that D. & M. came into financial difficulty.

An apprehension of this kind on the part of a small business set-up, transacting, nonetheless, a disproportionately large volume of affairs, surely does not seem exaggerated. Similar protective steps are resorted to so frequently, apart from any ethical considerations, that such "hedging" practices cannot escape judicial notice. This commercial foresight is plainly outlined at pages 5 and 6 of the appellant's Summary of Argument; quote:

> (a) D. & M. carried on a substantial volume of sales of plywood etc., over $1,000,000 a year, on a very small working capital. It sold to builders and others in the construction business and its accounts receivable were large and frequently overdue. Its risk of large credit losses was great and the failure of even one or two large customers could have resulted in disaster.
>
> (b) Accordingly, it made the best possible sense for the real estate which was bought in 1959 to be purchased in a corporation other than D. & M. Building Supplies, in order to protect it from any hazards of the D. and M. business and ensure that if the Rosenberg family lost their money in the D. & M. business they would still have this property.

Good and true, doubtless, if the one and only permissive condition stipulated by statute is not defeated by counter-evidence, in which case, two or more corporations, though not associated according to section 39(4)(*c*), "shall, if the Minister so directs, be deemed to be associated with each other in the year" conformably to section 138A, s.s. (2) (*b*) and s.s. (3)(*b*)(ii). The distinctive legal or corporate identity of those two or more companies persists only if and when none of the main reasons for their separate existence "is to reduce the amount of tax that would otherwise be payable under this *Act*". A pure and simple question of facts, to be determined in the light of the evidence adduced. I agree with appellant's learned counsel, as stated on page 5 of his Summary of Argument, that "the proper test is...if one supposed that all corporations were subject to tax at a flat rate of 50%, as has been recommended by the Royal Commission on taxation, would it be expected that these particular operations would have been carried on by separate corporations".

Mrs. Doris Rosenberg, the only witness heard by the appellant, was examined and cross-examined at great length.

I now refer to my notes, on the topic of the organization and dealings of Doris Trucking Company, Limited, since the other salient parts of Mrs. Rosenberg's deposition are fairly reported in the excerpts cited from the memorandums of both parties.

"Until 1958, Mrs. Rosenberg owned shares in the joint concern, D. & M., which she sold to her husband at a stipulated price of $12,500, upon the incorporation of Doris Trucking Co. Ltd., November 19, 1958. Shortly afterwards, December 1st, 1958, the recently incorporated company took over the working crew, formerly in the employ of D. & M., and also its three delivery trucks that were paid for later by Doris Rosenberg. This state of affairs meant that D. & M. carried on its trade solely through the instrumentality of Doris Trucking Co., which, in turn, was unionized in August, 1963. Each company had its own bank account".

We now reach a more informative and significant phase of evidence. "Despite her ownership of Doris Trucking, of which she was President and sole shareholder, Mrs. Rosenberg continued working, five days a week, in the credit department of D. & M.; Doris Trucking Company is not listed in the Toronto telephone book; D. & M. Supplies being the registered party, at civic number 229 Wallace Avenue, a building owned by Mrs. Rosenberg who charges

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no rental whatsoever to D. & M. Nowhere does the name of Doris Trucking Co. appear at 229 Wallace Avenue, nor does it affix any commercial advertisement and has no business stationery. On the three trucks only, says the witness, a marking reads 'owned and operated by Doris Trucking Co. Ltd.'. From December 1st, 1958, repeats Mrs. Rosenberg, Doris Trucking has attended to all business requirements of D. & M. to which regular charges are made for trucking, deliveries and other services rendered by the appellant". She adds that corresponding payments were made by D. & M. to Doris Trucking. Mrs. Rosenberg Draws no pay from her own company but receives a considerable remuneration from D. & M. In 1964 the salary and bonus paid to her by D. & M. amounted to $16,330 (*cf* Ex. 1, Tab. 1, page 5). She agrees that the prospect of lesser income tax dues was casually referred to in the course of consultations with the companies' accountant.

Let us now inquire into the admissible plausibility of the known reasons invoked by appellant in vindication of its submission that "none of the main reasons for the separate existence of the two...companies is to reduce the amount of tax that would otherwise be payable under this *Act*".

And let us also keep in mind as a guide-line that the onus of proof resting upon the appellant, should any substantial doubt arise regarding the adequacy of such proof, its benefit must necessarily accrue to the taxing authority.

The respondent's reply to appellant's first allegation, in keeping with the proven facts, disposes of the rather shallow ground of eventual labour troubles. I now quote from pages 5 and 6 of Mr. Mogan's Notes of Argument:

> It was brought out in evidence that the premises at 229 Wallace Avenue had only three entrances which could be used by trucks and which might be sealed off by picketing in order to prevent strike-breaking drivers from using the vehicles owned by the employer (Doris Trucking) to make deliveries for D. & M.
>
> There was no other business premises used by Doris Trucking and we can only assume that the head office of Doris Trucking was integrated with the office of D. & M. at 229 Wallace Avenue. On the evidence we have no reason to believe and there is no assurance that D. & M. could go into the labour market and hire "strike-breaking" drivers and yardmen in the event of a strike against Doris Trucking, when it would be so obvious—particularly to the striking employees of Doris Trucking—that the two companies are closely related and do in fact work together.

> ...On the evidence, the most logical inference to draw is that a strike by the employees of Doris Trucking would in fact close down the business of D. & M....

It seems hard to disagree with this reasoning, especially so in connection with people, such as appellant's President, so acutely awake to the thoroughness of labour practices in the highly unionized region of Metropolitan Toronto. Yet, I will go so far as to concede that this dubious and surprisingly ingenuous scheme may have been one of the reasons "for the separate existence" of the companies, but not to the exclusion of others, as for instance, the second one (*supra*) advanced by Doris Trucking and commented upon at pages 7 and 8 of respondent's Notes of Argument in these lines:

> To summarize Mrs. Rosenberg says that the land (i.e. the $23,500 real estate purchase in Trafalgar Township) was put into Doris Trucking to keep it free from any potential action of the creditors of D. & M. And yet, at the commencement of 1964, the year under appeal, Doris Trucking had an unsecured loan receivable from D. & M in the amount of $30,000; and during 1964, Doris Trucking loaned to D. & M. an additional $2,000 so that at the end of 1964, Doris Trucking had a loan receivable from D. & M. in the amount of $32,000.

Respondent's counsel next infers that:

> When faced with these facts, I suggest that the alleged second reason for the existence of Doris Trucking in 1964, (that is to hold the land free and secure from D. & M.) is not a reason which this Court should accept because the same person, Doris Trucking, who is supposedly holding the land secure from the creditors of D. & M., has loaned to D. & M. throughout that year the amount of $30,000; a loan which is greater than the value of the land.

Another questionable factor raises doubt as to this assertion of appellant. The evidence reveals that Doris Trucking's entire business activities were concentrated upon D. & M., its only client, from which it consequently derived its one regular source of income, i.e. the wages paid to the drivers and yardmen it kept at D. & M.'s constant disposal, plus the cost of the three trucks engaged in the trade deliveries of this latter firm. Still, it is strange and unexplained, as revealed by Exhibit 1 (Tab. 1, page 6) and discussed at pages 9 and 10 of respondent's notes that:

> (4) The amounts paid by D. & M. to Doris Trucking exceeded the wages that were payable to the drivers and yardmen and the cost of operating the trucks. We know this to be true because the rental of

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trucks, drivers and yardmen to D. & M. was the only business carried on by Doris Trucking and Exhibit 2 demonstrates that throughout the period of 1959 to 1965, Doris Trucking earned the following profits:

YEAR	PROFIT
1959	$12,227 40
1960	10,033 30
1961	17,572 82
1962	12,658 16
1963	16,456 63
1964	14,198 72

We can therefore see, continues Mr. Mogan, that D. & M. (by paying amounts to Doris Trucking which exceed the wages of drivers and yardmen, and the costs of operating the trucks) has had greater amounts to deduct in computing its income since 1958 with respect to its delivery service than it would have had if Doris Trucking had not been incorporated. These greater amounts paid by D. & M. to Doris Trucking, have the effect of reducing the (taxable) profit of D. & M. while at the same time accumulating a separate profit in Doris Trucking.

Since 1960, the rate of tax payable by a corporation is established thus by section 39(1) of the Act:

18% on the first $35,000 00 of revenue and 47% on all profits exceeding $35,000.00.

Therefore, the advantage of separate companies operated, either by the same family or by closely related interests, becomes readily perceivable. If not associated a group of companies can each pay income tax at the rate of 18% on the first profit amount of $35,000 respectively earned. Whereas, if associated, then, the rate of taxation at 18% applies only to the initial $35,000 of their joint income.

In the case at bar, the first eventuality just stated would mean for the appellant an income tax reduction of $4,117.63.

If Doris Trucking, *alias* Mrs. Rosenberg feared, as she told the Court, the several commercial risks incurred by her husband's company, to the point that she resolved to sever any responsibility with D. & M. Builders' Supplies, and seek legal refuge in her own separate firm, she managed, with remarkable celerity, to keep such anxiety under firm control, as shown by her acceptance of an enduring and unsecured loan to D. & M., the "danger spot", of $32,000 still outstanding in 1964.

That does not mean that I brush aside Mrs. Rosenberg's assertion, notwithstanding its limping logic. It stands to reason that in the event (quite an improbable one) of D. & M.'s insolvency, she should endeavour to save the most she could, but this natural impulse was coupled with risking a good deal of cash. But is it then improbable that the combined business acumen of Mrs. Rosenberg and her employer-husband might not have insinuated some gradual set-off, a yearly amortization of the unsecured loans from appellant to D. & M., by the tax reducing means of separate companies I suppose no blame attaches to even a perfervid zeal for thrift, and Doris Trucking took advantage at full stretch of this prevalent striving. On page 3 of J. F. Spencer's report, dated April 17, 1966 (Ex. 1, Tab. 1), filed with the consent of both parties, we read that:

Doris (Trucking Company) charges D. & M. at the following rates:

	DRIVER (Including the truck)	YARDMEN
1958	$3.50 per hour	$1.75 per hour
June 1960-July 1962	3.75 " "	1.85 " "
Aug. 1962	3.80 " "	1 90 " "
Sept. 1962-Dec. 1964	3.85 " "	1 95 " "
Jan. 1965	3.95 " "	2 05 " "

"These rates," states Mr. Spencer in his report, "are below a fair market value. This was verbally admitted by L. Kirshenbaum, auditor"; presumably the Rosenberg's auditor.

Assuredly, the Rosenberg couple kept a wary eye on every source or streamlet of gain, to such a degree that a saving of $4,117.63, in 1964, may not have escaped the statute's truly tentacular reach in being "one of the main reasons" for the separate existence of each company.

Appellant's counsel, Mr. Goodman, made reference to a recent decision of the House of Lords under the United Kingdom income tax law, *in re Commissioners of Inland Revenue v. Brebner*[1], the facts of which are summarized on pages 9 and 10 of his Summary of Argument from which I quote:

...The taxpayer (Brebner) engaged in a number of transactions with a company in which he was interested as a shareholder and a

[1] [1967] 1 All E R 779, at pages 781, 783, 784.

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director, and the purpose of the transactions was to defeat a take-over bid. One of the transactions was the capitalization of some of the reserves and the application of the resulting sum in paying up ordinary shares which were allotted to the shareholders among whom was the taxpayer.

The Inland Revenue served on the taxpayer a counteracting notice under Section 28 of the Finance Act 1960, contending that that particular transaction had as its main object or one of its main objects to enable the shareholders to obtain a tax advantage. It was contended for the taxpayer that the only purpose of the transaction was to defeat a take-over bid. The Special Commissioners decided in favour of the taxpayer and the House of Lords confirmed their finding.

There are, I believe, important dissimilarities with the circumstances leading up to the cited case and the instant one.

The corroboration sought by the appellant is, supposedly derived from the speeches of Lord Pearce and Lord Upjohn, the former writing at page 781 of the report that:

> The subsection (28) would be robbed of all practical meaning if one had to isolate one part of the carrying out of the arrangement, namely the actual resolutions which resulted in the tax advantage, and divorce it from the object of the whole arrangement. The method of carrying it out was intended as one part of a whole which was dominated by other considerations.

Then, by Lord Upjohn at page 784:

> I agree that the question whether one of the main objects is to obtain a tax advantage is subjective and, as Lord Greene, M.R., pointed out in Crown Bedding Co., Ltd. v. Inland Revenue Comrs. (1 All E.R. 452 at pp. 453, 454) is essentially a task for the Special Commissioners unless the relevant Act has made it objective (and that is not suggested here).

The eminent jurist concludes his pronouncement in the undergoing terms:

> My Lords, I would conclude my judgment by saying only that, where the question of carrying out a genuine commercial transaction, as this was, is considered, the fact that there are two ways of carrying it out—one by paying the maximum amount of tax—the other by paying no, or much less, tax—it would be quite wrong as a *necessary* consequence (emphasis in text) to draw the inference that in adopting the latter course one of the main objects is for the purposes of the section, avoidance of tax. No commercial man in his senses is going to carry out commercial transactions except on the footing of paying the smallest amount of tax involved. The question whether in fact one of the main objects was to avoid tax is one for the Special Commissioners to decide on a consideration of all the relevant evidence before them and the proper inferences to be drawn from that evidence.

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Of course I am in respectful agreement with all that precedes; namely that similar issues are a pure question of fact; that no one can be expected to commit fiscal "*hara-kiri*", and, lastly, the truism that the case must be dealt with in a subjective light. Yet, this subjective approach remains within the scope of judicial scrutiny.

Should the evidence fail to dispel the doubt, and so it does in my humble opinion, that "none of the main reasons for the separate existence of the two pertinent corporations is to reduce the amount of tax that would otherwise be payable under this Act", the appellant cannot succeed.

This appeal is therefore dismissed with all taxable costs recoverable by the respondent.

Winnipeg 1968 Apr. 23 | Ottawa May 21

BETWEEN:

GABCO LIMITED .... APPELLANT;

AND

THE MINISTER OF NATIONAL REVENUE .... RESPONDENT.

Income tax—Remuneration of employee—Salary and bonus proportionate to shareholding—Whether amount reasonable—Income Tax Act, s. 12(2).

Appellant, a construction company, remunerated its manager and eight other permanent employees, who held 73% of the issued capital stock of the company, in a manner commensurate with their estimated value to the company, by a modest salary plus a bonus proportionate to shareholding. The remaining 27% of the issued capital stock was held in trust for the manager's minor brother, who was not an employee. In 1962 appellant employed the manager's brother with a view to his becoming the manager's principal assistant under the above arrangement as to remuneration. In 1962 he was paid $851 salary and $19,520 bonus for three months' work, and in 1963 he was paid $5,280 salary and $30,393 bonus for a full year's work. In computing appellant's income for those years the Minister, applying s. 12(2) of the *Income Tax Act,* disallowed as an expense remuneration paid the manager's brother in excess of $3,600 in 1962 and of $7,200 for 1963 on the ground that remuneration paid him in excess of those amounts was not reasonable in the circumstances.

Held, allowing the appeal, the evidence as to the considerable value of the services of the manager's brother indicated that his remuneration was reasonable in all the circumstances. It is not for the Minister or the court to substitute its judgment as to what is reasonable remuneration. The question is rather whether a reasonable business man would have paid such an amount having only business considerations in mind.

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In fixing the remuneration at the outset appellant was not restricted to the value of the employee's immediate services but might have future benefits in mind.

INCOME TAX APPEAL.

Walter Newman, Q.C. for appellant.

F. J. Dubrule and *J. M. Halley* for respondent.

CATTANACH J.:—These are appeals from the appellant's assessments to income tax for its 1962 and 1963 taxation years which coincide with the calendar years.

The appellant is a joint stock company incorporated pursuant to the laws of the Province of Manitoba by letters patent dated June 15, 1960, under the name of G. A. Baert Construction (1960) Ltd. By supplementary letters patent dated September 29, 1965, the corporate name was changed to Gabco Limited as is recited in the above style of cause.

The purpose of the incorporation of the appellant was to purchase and carry on a general construction business previously carried on by G. A. Baert Construction Co. Limited. This predecessor company was begun by G. A. Baert who was an immigrant from Belgium with no academic training beyond the equivalent of grade V, but he was a skilled carpenter. He founded the company of which he was the president and general manager and from 1950 forward until 1960 he was assisted in its management by his eldest son, Jules.

The company became one of the five largest and most successful construction businesses in the City of Winnipeg. In every year of its operation it earned a profit in excess of $100,000 and built some of the most imposing edifices in the City of Winnipeg such as the Great West Life Building, the Norquay Building which is a Provincial Government building, some of the buildings of the University of Manitoba and many other buildings.

The father, G. A. Baert was predominant in the management of the company's affairs but came to rely heavily upon his son Jules for assistance who gradually assumed the predominant role.

In 1960 the father suffered a severe coronary attack. Therefore the appellant was incorporated of which Jules became the major shareholder and president and managing director. By an agreement dated January 1, 1961, the appellant purchased all the assets of G. A. Baert Construction Co., Ltd. and assumed all its liabilities for a total purchase price of $1,243,223.41. The assets so purchased included all contracts, work in progress and accounts receivable to the total value of $1,158,152.32 and the liabilities assumed were in the amount of $841,899.55.

The subscribed and paid up capital of the appellant in 1962 was $500,500 of which $500,000 was for fully paid preferred shares and $500 was for fully paid common shares.

The shareholders were as follows:

	Preferred	Common	Value
Jules Baert	24,300	243	$243,243.00
Robert Baert	12,200	122	122,122.00
John Jackson	5,000	50	50,050.00
Geo. F. Chaput	2,000	20	20,020.00
Alfred Giavendini ..	1,500	15	15,015.00
William A. Balgals ..	1,000	10	10,010.00
Laugi Helgason	1,000	10	10,010.00
Eugene S. Mager ..	1,000	10	10,010.00
Robt. M. Sutton	1,000	10	10,010.00
Romer N. Verrier ..	1,000	10	10,010.00
	50,000	500	$500,500.00

At the inception of the appellant there appears to have been 50 fewer preferred shares issued, but I would assume that they were issued in the interval. The foregoing proportions as above outlined remained constant throughout the taxation years under review.

The sole managerial responsibility in this highly competitive business fell upon Jules Baert. He assumed responsibility for estimating competitive bids to be made for contracts, the purchasing of materials and the supervision of sub-trades and labour relations. If a bid were too high it would be unsuccessful and if it were too low, and it were accepted as would be likely, then disaster would result. In his view he was unable to delegate any of his responsibilities. The next senior employee was John Jackson, who is described as a certified engineer by which I assume is

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meant a person without the academic qualifications of professional engineer but with practical experience. In Jules Baert's opinion Mr. Jackson's capabilities were limited to actual job supervision and he was not qualified by temperament or otherwise to undertake management duties.

When the appellant was organized it was decided as a matter of policy that employees of a permanent nature should be allowed and invited to participate in share ownership undoubtedly as an incentive to greater efforts to further the progress of the appellant. It was also decided as a matter of policy that the extent of share ownership of each particular employee would be limited to a proportion commensurate with that employee's contribution to the welfare of the appellant company. All employees agreed to participate in this arrangement and the implementation thereof is reflected in the list of shareholders and holdings which I have set out above.

The remuneration of the employee-shareholders as listed above was also the subject of a special and somewhat unusual arrangement. Each employee was paid a comparatively modest salary but at the end of each fiscal year a bonus was declared and divided among the employees proportionate to their share ownership. The total of the salary and the share of the bonus constituted the annual remuneration of the employees. I might add that in certain material tendered in evidence, I have observed that the shareholders also received dividends which I presume were declared on the preferred shares although there was no evidence adduced to that effect.

By an agreement dated March 9, 1961, among all the shareholders, Walter C. Newman as trustee for Robert Baert and Elaine Baert and the appellant it was agreed that in the event of termination of the employment of any shareholder, whether voluntarily or involuntarily, other than Jules Baert and the trustee, the shares of that holder should be offered to the other employee-shareholders *pro rata* to the number of shares held, but if any shares so offered are not acquired then those shares would be acquired by Jules Baert. It was also agreed that no additional shares would be issued without the concurrence of all shareholders.

The only shareholder of the appellant who was not an employee at the time of the issue and allotment of shares was Robert Baert, the youngest son of G. A. Baert and a younger brother of Jules.

G. A. Baert subscribed and paid for 12,200 preferred and 122 common shares in the appellant which were held in trust for Robert Baert and his sister Elaine. On January 1, 1962, G. A. Baert arranged that Elaine's shares should be purchased by Robert and the proceeds were used to purchase a revenue bearing property for Elaine thereby affording her a secure income and absolving her from any participation in the contracting company, the appellant. Therefore as at January 1, 1962, Robert became the beneficial owner of all of the shares indicated and for the purposes of these appeals he may be considered as the registered owner which he did in fact become on July 6, 1964, after reaching his majority.

It is quite obvious that G. A. Baert, who was faced with the prospect of imminent death, was making provision for the future of his children during his lifetime.

He advanced funds to Jules which were used by him to acquire controlling ownership of shares in the appellant and all indications were that Jules' success was assured. He had made provision for Elaine so that only Robert's future remained to be considered.

As a child of 10 and onwards through the years he had been temporarily employed in his father's construction businesses in a variety of minor jobs.

In 1960 or thereabouts, he served as "the eyes and ears" of Jules in connection with the construction of Edinburgh House, a $1,600,000 project in a position of nominal subservience to the superintendent on the site. His responsibility was to "finish up" each suite prior to its occupancy which duty he discharged to the satisfaction of his brother and father.

In 1961 he failed his year at St. Paul's College for the second time and was denied admittance to a school in the United States. His academic career was not successful but neither was that of his brother Jules who had failed first year Arts and first year Engineering at University before entering his father's business at age 19.

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Meanwhile Jules, who wished to delegate some of his onerous duties was looking for a number two man, and he saw that man in his brother Robert. Since Jules was willing to accept Robert, the father then arranged for the transfer of Elaine's shares to his brother Robert.

As a step in Robert's preparation for his proposed status in the appellant to which he would be entitled by his share ownership he was employed by the appellant's legal advisors at a monthly salary of $50.00 to learn some of the legal aspects of the construction business.

In October 1962 at the age of 19 Robert entered into full time employment with the appellant at a monthly salary of $300 and participation in the bonus arrangement on the basis of his shareholding with the tacit concurrence of the other shareholders.

His first assignment was as assistant superintendent on the construction of the Winnipeg City Hall, the cost of which was in excess of $6,000,000. The building was completed ahead of schedule and when the building was "closed in" Robert went on to other duties. While at the City Hall site he made innovations in masonry construction which resulted in the speeding up of construction at a substantial saving. Here again he acted as "the eyes and ears" of his brother Jules or as liaison between the site and the office. He was given the title of assistant superintendent as a matter of discretion in deference to age and experience of the superintendent with whom some difficulties were beginning to be encountered.

In 1962 the appellant performed gross contracts in the amount of $4,203,621.09 and in the year 1963 in the amount of $7,800,724.41.

The net profits of the appellant in those two years were respectively $191,131.96 and $211,531.45.

In 1962 salaries and bonuses were in the amount of $128,770.09 and in 1963 in the amount of $173,981.86.

In the year 1962 Robert received $851.39 in salary and $19,520 as bonus for a total remuneration of $20,371.39 which he reported as income and paid tax thereon.

In the year 1963 he received $5,280 in salary and $30,393 as a bonus for a total remuneration of $35,673 which he reported as income and paid tax accordingly.

In assessing the appellant as he did for its 1962 and 1963 taxation years the Minister did so on the assumption set out in his reply to the Notice of Appeal, that

(*a*) during its 1962 and 1963 taxation years the appellant paid to Robert Baert on account of salary the following amounts:

Year	Months employed	Total salary paid	Average salary per month
1962	3	$20,371.39	$6,790.46
1963	12	35,673 00	2,972.40

(*b*) the extent to which the salary paid to Robert Baert was reasonable in the circumstances, was as follows:

1962	$1,800 00
1963	7,200.00

The Minister, therefore, concluded that the deductions claimed by the appellant in respect of an outlay or expense on account of remuneration paid to Robert Baert in 1962 and 1963 for the purpose of gaining income from its business were not reasonable in the circumstances, within the meaning of section 12(2) of the *Income Tax Act* to the extent that they exceeded the sums of $1,800 and $7,200 during the appellant's 1962 and 1963 taxation years.

The Minister re-assessed the appellant by adding back to the appellant's income the amount of remuneration paid to Robert Baert in excess of $3,600 in 1962 (which amount is at variance with the amount of $1,800 set out in the Notice of Reply) being $16,771.39 with the result that the disallowance increased the appellant's tax for that year by $8,553.40 plus $833.62 in interest. Similarly for the year 1963 the Minister added back to the appellant's income for that year, the remuneration paid to Robert Baert in excess of $7,200 being $28,473 which increased the appellant's tax by $14,521.24 plus $811.67 in interest.

Section 12(1)(*a*) of the *Income Tax Act* provides as follows:

12. (1) In computing income, no deduction shall be made in respect of

(*a*) an outlay or expense except to the extent that it was made or incurred by the taxpayer for the purpose of gaining or producing income from property or a business of the taxpayer.

Subsection (2) of section 12 provides:

(2) In computing income, no deduction shall be made in respect of an outlay or expense otherwise deductible except to the extent that the outlay or expense was reasonable in the circumstances.

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The appellant contends that the payment of remuneration to Robert Baert was made in the ordinary course of the business of the appellant and was an expense incurred for the purpose of gaining income. This the Minister does not dispute.

The appellant further contends that the remuneration paid to Robert in the taxation years in question was reasonable in all the circumstances, which contention the Minister does emphatically dispute, and herein lies the crux of the issue between the parties.

In support of his submission that the remuneration received by Robert in 1962 and 1963 was unreasonable in the circumstances, counsel for the Minister specifically pointed out Robert's extreme youth, his academic failures, that his compensation for the six months' work he did for appellant in 1961 (i.e. the finishing of Edinburgh House) was only $1,409.80, that he worked for the appellant's solicitors in 1962 for $50 per month and that his remuneration for the last three months of 1962 as assistant superintendent on the construction of the Winnipeg City Hall, was far in excess of that received by John Jackson, the general manager of the appellant and superintendent on that job.

The portion of the remuneration received by Robert in 1962 and 1963 allocated to salary was exceeded by every other employee-shareholder. However the bonus portion of his remuneration in those years based upon share ownership greatly exceeded that of every other employee-shareholder excepting his brother Jules (see Exhibit 9).

I can see no legal impediment to the appellant basing the greater bulk of the remuneration paid to its employees who were shareholders upon a declared bonus in successful years divided among them *pro rata* according to their shareholdings. This was the understanding and agreement on which those employees (including Robert Baert) entered the employ of the appellant. Under ordinary corporate principles I should have thought the same result could have been accomplished by the declaration and payment of dividends on the common shares except that the amount of the dividends declared and paid would be income in the hands of the appellant and taxable accordingly rather than deductible as an expense laid out to earn income. However it was not raised in argument nor in the pleadings that the appellant was precluded from making the arrangement that it did with its employees.

The ultimate test as to when a payment is *intra vires* a company is when what is done is done *bona fide,* within the ordinary scope of the company's business and reasonably incidental to the carrying on of the company's business for the company's benefit and advantage.

Long ago Bowen L.J. said in *Hutton v. West Cork Co.*[1]:

> A company which always treated its employees with Draconian severity, ... would soon find itself deserted .. The law does not say that there are to be no cakes and ale, but there are to be no cakes and ale except such as are required for the benefit of the company.

The arrangement between the appellant and its employees to pay bonuses according to their shareholdings was, in my view *bona fide,* within the scope of the appellant's business and incidental to the carrying on of that business for the appellant's advantage. I should think that it is for the appellant, through its directors, to decide that such an arrangement was in the interests of the appellant subject only to the limitation that it is reasonable in the management of the appellant's affairs.

The Minister did not attack the arrangement for bonus payments *per se* as being unreasonable, but only the payment to Robert Baert on the grounds that such payment was not commensurate with the value of his services and contribution to the appellant.

The allocation of shares by the appellant to its employees was predicated upon an evaluation of the contribution that each employee would make to the appellant's benefit based upon the performance of such employees in the predecessor company. As intimated before, the only exception to the allocation of shares on such basis was Robert Baert who was not an employee of the appellant at that time. He obtained his shares in the circumstances outlined above that is as a consequence of the purchase of them by his father as a provision for Robert's future and in the contemplation of his eventual participation in the affairs of the appellant subject to his brother Jules' concurrence. It was a term of Robert's

[1] (1883) 23 Ch. 654.

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employment by the appellant in October 1962 that he would participate in any bonuses *pro rata* according to his shareholding and this was with the full approval of his brother Jules and the tacit approval of the other shareholders. It therefore follows that Robert's remuneration by way of bonus would have been the same as it was regardless of the value of his services to the appellant.

For the reasons above indicated, I am of the opinion that the arrangement for the payment of bonuses to the employees of the appellant *pro rata* to their shareholdings is *intra vires* the appellant, that the scheme was a reasonable one within the competence of the appellant or its directors to make and accordingly the bonuses as a whole qualify as a deductible expense within the meaning of section 12(1)(*a*) of the *Income Tax Act.*

However, in my opinion, the Minister is entitled to consider the salaries and bonuses paid individually and separately (he is not restricted to considering the bonuses "in toto") and to enquire if the remuneration paid to Robert was out of proportion to the value of his services to the appellant and if so to disallow the disproportionate part on the ground that such payment was really a distribution of taxable profit in the guise of remuneration for services rendered. On the other hand, reasonable remuneration should not be interfered with.

The greater bulk of the evidence adduced on behalf of the appellant was directed to demonstrating that the value of the services performed by Robert justified the remuneration paid to him.

Jules Baert testified that the services performed by Robert, even from the outset of his employment, were such as could not be performed by any of the other employee-shareholders including the most senior one, John Jackson who held the title of general manager. It was Jules Baert's plan that Robert would serve as backup man to himself and relieve him of much of his responsibility. Even from the beginning of Robert's employment he was with his brother constantly rendering whatever assistance required of him. His initial assignments were on the sites of the appellant's projects to act as an energetic driving force to bring each project to its scheduled completion on or before the date thereof in which he was successful. While his title may have indicated subservience to the superintendent on a particular job, nevertheless, he was in reality the senior person because of the direct channel between him and his brother.

In 1964 the appellant engaged Profit Counselors Inc. a firm of management consultants to review and advise upon its organizational structure, to evaluate its personnel as well as to install systems of integrated costing and estimating. Arthur Firus, an officer the consultants engaged, conducted the review and his opinion confirmed that of Jules' that Robert was in fact the number two man in the appellant and was functioning as such at that time. His recommendation was that Robert should be confirmed in that position in name as well. This recommendation was implemented and John Jackson was discharged.

Mr. Firus testified in glowing terms of the efficiency and success of this brother team. In his opinion it was the best he had ever encountered. I am conscious of the fact that the opinion of Mr. Firus is self-serving to a certain extent. His employer sold its services to the appellant by solicitation. His recommendations supported the facts as he found them with respect to personnel and with organization as had been instituted by Jules in the top level of management. I cannot disabuse my mind of the impression that the consultants were engaged as a prop to rid the appellant of its general manager who was the nominal number two man and replace him with Robert as was done. However, it is clear from Mr. Firus' evidence that he found the brother team had been extremely successful and had worked harmoniously and that such success was reflected in the continued success of the appellant. I also accept the testimony of Mr. Firus that the salary of the second senior officer of a construction company is normally 70 per cent of that of the senior officer. The remuneration that Jules received in 1962 was approximately $48,000. The remuneration of the second officer on that basis would be approximately $32,-600. In 1962 Robert received $20,371.39 made up of $851.39 in salary and a bonus of $19,520 which is less than 70 per cent of the salary of the senior man but I have not overlooked the fact that he was only employed for three months in that year. The explanation for such high

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remuneration for this short period of employment is his proportionate part of the bonus based on his shareholding.

In 1963 Jules received a remuneration of $57,626. Seventy per cent of that figure would be $40,334 and Robert received $35,673 as remuneration.

I have no difficulty in concluding that Robert's remuneration in 1963 was reasonable in all the circumstances.

By means of a graph and working backwards Mr. Firus expressed the opinion that Robert's salary in 1962 on his worth to the appellant would have been about $10,000. The working of such a projection backwards was not explained to my satisfaction. However Jules saw in his brother, Robert, great potential which foresight was demonstrated by subsequent events to have been well founded. While I have no doubt that the likelihood of Robert being employed by the appellant had he not been Jules' brother and G. A. Baert's son was remote and if it were not for the fact that he owned 12,200 preferred and 122 common shares in the appellant, his remuneration in 1962 would not have been $20,371.39, nevertheless, in view of his contemplated status in the appellant company, which he subsequently fulfilled, it cannot be said that his contract of employment with the appellant and the consequent remuneration was unreasonable in all the circumstances. I might add that subsequent to the reorganization of the appellant in 1964, the share bonus arrangement with its employees was abandoned, the shares of the employees other than Jules and Robert were acquired by them so that Jules and Robert held all issued and outstanding shares equally.

It is not a question of the Minister or this Court substituting its judgment for what is a reasonable amount to pay, but rather a case of the Minister or the Court coming to the conclusion that no reasonable business man would have contracted to pay such an amount having only the business consideration of the appellant in mind. I do not think that in making the arrangement he did with his brother Robert that Jules would be restricted to the consideration of the service of Robert to the appellant in his first three months of employment being strictly commensurate with the pay he would receive. I do think that Jules was entitled to have other considerations present in his mind at the time of Robert's engagement such as future benefits to the appellant which he obviously did.

Accordingly, it cannot be said, in view of all the circumstances, that the contract of employment here in question was not a reasonable one actuated by reasonable business considerations and to the ultimate advantage and benefit of the appellant.

It follows that the appeals herein are allowed with costs.

Ottawa
1968
May 17
June 7

BETWEEN:

STANDARD OIL COMPANY ....APPELLANT;

AND

THE REGISTRAR OF TRADE MARKS .... RESPONDENT.

Trade marks—"Fior", an invented word—Whether primarily merely surname of individual—Test to apply—Rejection of application for registration—Affidavit filed by Registrar—Admissibility of—Evidence on appeal—Trade Marks Act, s. 12(1)(a), 55(5), 58(3)—Exchequer Court Rule 36(6).

An application for registration of the trade mark "FIOR" (made up of the initial letters of the words "fluid iron ore reduction") for use with appellant's wares was rejected by the Registrar of Trade Marks as being "a word primarily merely the surname of an individual" and therefore not registrable under s 12(1)(*a*) of the *Trade Marks Act*. Appellant appealed to this court. The Registrar filed an affidavit on the appeal pursuant to *Exchequer Court Rule* 36(6) declaring that "FIOR" appeared in Montreal's directory as the surname of one individual in 1955, in Toronto's for nine individuals in 1967, and similarly in a number of U S directories.

Held, the appeal must be allowed.

"FIOR", though without dictionary meaning, is a word for trade mark purposes, but to the general public of Canada it is not primarily merely the surname of an individual, which is the test to apply. *Magnolia Metal Co's Trade Marks* (1897) 14 R P.C. 265, applied.

The Registrar was entitled to conclude from the city directories that "FIOR" was the name of one or more living individuals in Canada.

On appeal from the Registrar this court is entitled to receive evidence in addition to that which was before the Registrar. *Rowntree Co. v. Paulin Chambers Co.* [1968] S.C R. 134 considered; *Benson & Hedges (Canada) Ltd. v. St. Regis Tobacco Corp.* [1968] 2 Ex. C R. 22 referred to.

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APPEAL from Registrar of Trade Marks.

R. Graham McClenahan for appellant.

André R. Garneau and *H. A. Newman* for respondent.

JACKETT P.:—This is an appeal from a decision of the Registrar of Trade Marks rendered on November 14, 1967, refusing an application by the appellant for registration of the trade mark "FIOR" on the basis of its proposed use in Canada by the appellant in association with wares described in the application as "direct reduction iron ore".

The application was filed September 9, 1966, by Messrs. Gowling, MacTavish, Osborne & Henderson, as "Agents" for the appellant, and that firm was notified by a communication dated December 14, 1966, from the Trade Marks Office that "FIOR" was considered to be primarily merely the surname of an individual and that in view of the provisions of section 12(1)(*a*) of the *Trade Marks Act*, which reads as follows:

> 12. (1) Subject to section 13, a trade mark is registrable if it is not
>
> (*a*) a word that is primarily merely the name or the surname of an individual who is living or has died within the preceding thirty years;

it did not appear to be registrable.[1] As a result of an invitation issued to Gowling, MacTavish, Osborne & Henderson by that communication for their comments, an exchange of correspondence ensued during which, counsel are agreed, the respondent expressed his ultimate position by that part of his letter of May 8, 1967, that reads:

> Since the word "FIOR" has no dictionary meaning and appears in the directories of Toronto and Montreal as a surname, it is

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[1] In considering the interpretation of section 12(1)(*a*) adopted by the respondent, and in considering what effect should be given to it, it must be read with section 12(2) which reads:

> (2) A trade mark that is not registrable by reason of paragraph (*a*) or (*b*) of subsection (1) is registrable if it has been so used in Canada by the applicant or his predecessor in title as to have become distinctive at the date of filing an application for its registration.

In effect, what section 12(1)(*a*) prohibits is the registration of certain words as "proposed" trade marks When such word has been so used "as to have become distinctive", it may be registered as a mark that falls under section 2(*t*)(i).

considered to be primarily merely the surname of an individual. Therefore, the objection taken under section 12(1)(*a*) of the *Trade Marks Act*, is maintained.

(During the course of that exchange, the appellant filed affidavits of a professor of English, expressing the opinion that "FIOR" is not a word. In my view these affidavits are, in effect, an expression of opinion as to what the *ordinary* English word "word" means, and are not admissible evidence on what is a question of law. I see no indication that the Registrar paid any attention to them.)

As contemplated by Rule 36(2) of the Rules of this Court, when the appellant filed its Notice of Appeal in this Court on December 13, 1967, it also filed a statement of its "Allegations of Fact". As permitted by Rule 36(3) of those Rules, on January 23, 1968, the appellant filed an affidavit of one Francis X. Clair, the substantive paragraphs of which read as follows:

> 1 I am Trademark Counsel of the Standard Oil Company the Appellant herein, the said company being also the applicant for registration of the trade mark FIOR under application serial No. 299,506 filed in the Canadian Trade Marks Office and as such I have knowledge of the facts herein deposed to.
>
> 2. That the said trade mark FIOR was created by combining the first letters of each of the words "fluid iron ore reduction" and the mark has no meaning by itself.

A Reply and Allegations of Fact were thereupon filed on behalf of the respondent under Rule 36(4) and (5), and on February 7, 1968, an affidavit, sworn by the respondent himself, was filed as contemplated by Rule 36(6). This affidavit showed that "FIOR" appeared as the surname

(a) of one individual in Lovell's Montreal Directory (1955),
(b) of one individual in the Illinois Bell Telephone Directory (1967),
(c) of two individuals in the Pacific Telephone Directory for San Francisco (1966),
(d) of three individuals in the Pacific Telephone Directory for Los Angeles (1967), and
(e) of nine individuals in Might's 1967 Greater Toronto City Directory.

An application was thereupon made by the appellant on April 2, 1968, that the affidavit taken by the respondent

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"be struck out as inadmissible on the ground that it is not established in the affidavit that the information therein contained was available to and considered by the Registrar of Trade Marks in reaching his decision which is under appeal in these proceedings". This application was dismissed on the ground that it was not a proper case for making such an interlocutory application. (In my view, at that time, any question as to the relevancy or admissibility of evidence contained in affidavits filed under Rule 36 should be dealt with on the hearing of the appeal in the absence of special circumstances.)

At the opening of the argument of this appeal, the question was raised as to whether the appeal must, ordinarily, be determined on the basis of the evidence that was before the respondent when he made the decision appealed from, or whether the parties are entitled, as of right, to put evidence before the Court on the appeal that was not before the Registrar when he rendered the decision appealed from.

The *Trade Marks Act* imposes on the Registrar (the respondent) the duty of making many different classes of decision. We are concerned here with the duty imposed on him, at one of the several different possible stages in the processing of an application under section 29 for registration of a trade mark, by section 36(1), which reads as follows:

> 36 (1) The Registrar shall refuse an application for the registration of a trade mark if he is satisfied that
>
> (*a*) the application does not comply with the requirements of section 29;
>
> (*b*) the trade mark is not registrable; or
>
> (*c*) the applicant is not the person entitled to registration of the trade mark because it is confusing with another trade mark for the registration of which an application is pending,
>
> and where the Registrar is not so satisfied, he shall cause the application to be advertised in the manner prescribed.

In this case, the Registrar decided that the trade mark that the appellant had applied to have registered was "not registrable" and he therefore refused the application for registration of the trade mark as he was required, by section 36(1)(*b*), to do. The appeal from that decision was taken under section 55 of the *Trade Marks Act* which reads, in part:

> 55 (1) An appeal lies to the Exchequer Court of Canada from any decision of the Registrar under this Act within two months from

the date upon which notice of the decision was despatched by the Registrar or within such further time as the Court may allow, either before or after the expiry of the two months.

(2) The appeal shall be made by way of notice of appeal filed with the Registrar and in the Exchequer Court of Canada.

(3) The appellant shall, within the time limited or allowed by subsection (1), send a copy of the notice by registered mail to the registered owner of any trade mark that has been referred to by the Registrar in the decision complained of and to every other person who was entitled to notice of such decision.

* * *

(5) On the appeal evidence in addition to that adduced before the Registrar may be adduced and the Court may exercise any discretion vested in the Registrar.

This provision must be read with section 58, which reads:

58. (1) Where an appeal is taken under section 55 by the filing of a notice of appeal, or an application is made under section 56 by the filing of an originating notice of motion, the notice shall set forth full particulars of the grounds upon which relief is sought.

(2) Any person upon whom a copy of such notice has been served and who intends to contest the appeal or application, as the case may be, shall file and serve within the prescribed time or such further time as the court may allow a reply setting forth full particulars of the grounds upon which he relies.

(3) The proceedings shall then be heard and determined summarily on evidence adduced by affidavit unless the court otherwise directs, in which event it may order that any procedure permitted by its rules and practice be made available to the parties, including the introduction of oral evidence generally or in respect of one or more issues specified in the order.

Section 58(3) makes it clear that, unless the Court otherwise directs, such an appeal is to be "heard and determined" on "evidence" adduced by affidavit in this Court. This would seem to indicate that the statute contemplates the possibility that the evidence concerning the material facts (i.e., in this case, the facts material to the question whether the trade mark is "registrable") might be different from the evidence concerning the material facts that was before the Registrar. If that is so, the appeal to this Court does not necessarily raise a question as to whether the Registrar's decision was right or wrong because his decision might have been right on the evidence before him while the evidence before the Court on the appeal would require the Court to find different material facts and to reach a different conclusion. In other words, if that is the correct view of the matter, the appeal to this Court might be treated as being what is sometimes described as a "new

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trial". However, the wording of section 58(3) does not necessarily drive one to the conclusion that what is contemplated on the appeal is new evidence as to the facts that are material to the question that the Registrar decided. Bearing in mind that there is no provision, apart from section 58(3), as to the material on which an appeal should be decided, and assuming that the only appeal permitted by the statute is one restricted to the question whether the Registrar decided the question properly on the material that was before him, *evidence* would be necessary.

(a) as to what evidence was before the Registrar when he made his decision, and

(b) if an attack is made on the propriety of the decision as not having been made in accordance with fundamental principles, as to the facts surrounding the way in which the decision was reached;

and on that view, the reference to "evidence" in section 58(3), in the case of an appeal, would relate only to such evidence. That part of section 55(5) that provides that "On the appeal evidence in addition to that adduced before the Registrar may be adduced" might be explained as being consistent with either of these views as to the nature of a section 55 appeal. However, I am of the view that the provision for evidence "in addition" to that before the Registrar suggests very strongly that what is contemplated is "additional" evidence in relation to the same issues as the issues in relation to which evidence was adduced before the Registrar. It follows that, in my view, either party may put in evidence on the facts material to the issues that were before the Registrar and that such evidence may be considered along with the evidence that was before the Registrar, which, of course, must also be placed before the Court on the appeal.

In coming to this conclusion, I reject the suggestion that what is contemplated by section 55(5) is only evidence that was not available at the time that the matter was put before the Registrar. If that is what is contemplated, I should have thought that section 55(5) would be expressed as a discretion conferred on the Court to admit additional evidence such as is found in section 67 of the *Supreme Court Act*, R.S.C. 1952, chapter 259, and in Rule 234 of the Rules of the Supreme Court of Ontario.

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I do not, moreover, consider that I am in any way failing to give full effect to the decision of the Supreme Court of Canada in *Rowntree Co. v. Paulin Chambers Co.*,[2] concerning the effect to be given to the second part of section 55(5). As I indicated in a footnote to my judgment in *Benson & Hedges (Canada) Ltd. v. St. Regis Tobacco Corp.*[3], it does not seem to me that the effect to be given to the Registrar's exercise of discretion would be the same if, under section 55(5), there were adduced in this Court additional evidence that made a difference of substance between the facts before the Registrar and the facts before this Court.

My conclusion on the preliminary question raised at the hearing was, therefore, that this appeal was to be heard and determined on the material in the Registrar's file, a certified copy of which had been placed before the Court in accordance with the Rules of Court, and upon the affidavits that had been filed in this Court by the respective parties before the hearing in accordance with the Rules. I made an order accordingly. I might add that while counsel for the parties argued the question, both parties were of the view, as I understood them, that the question as to what evidence should be considered by the Court on this appeal should be resolved in the way that I have decided it.

I turn now to the merits of the appeal.

The appellant, as I have already indicated, applied for registration of the trade mark "FIOR" on the basis of its proposed use in Canada by the appellant in association with wares described in the application as "direct reduction iron ore". The respondent rejected that application on the ground that the trade mark in question was a "word" that is "primarily merely the surname of an individual" and was therefore "not registrable" by virtue of that part of section 12(1)(*a*) that provides that a trade mark is "registrable" if it is not "a word that is primarily merely . . . the surname of an individual who is living or has died within the preceding thirty years". The respondent's conclusion was based (see his letter of May 8, 1967) on two facts, *viz*:

(a) the word "FIOR" has no dictionary meaning, and

2 [1968] S C.R. 134.

3 [1968] 2 Ex C R. 22

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(b) the word "FIOR" appears in the directories of Toronto and Montreal as a surname.

By reason of these two facts, "FIOR" was considered by the respondent to be "primarily merely" the surname of an individual.

Two attacks by the appellant on the respondent's conclusion can be dealt with briefly. They are

(a) that the trade mark "FIOR" is not "a word" within the meaning of the word "word" where it appears at the beginning of section 12(1)(*a*) of the *Trade Marks Act*; and

(b) that the fact that "FIOR" appears in the directories of certain Canadian cities as a surname is not a proper evidentiary basis for concluding that it is the surname of an individual.

Dealing with the latter submission first, I think it is fair to say that the submission is based on the contention that "These compilations are not noted for their accuracy and we have no assurance that the surname relied upon has not been mis-spelled, nor do we know in fact whether it is an actual surname or only an assumed name having no legal effect or existence". This, in my view, goes to cogency, but not to relevancy. In my view, it was open to the respondent to conclude from the fact that "FIOR" has appeared in directories in Canada as a surname that the balance of probability is that "FIOR" is the surname of one or more individuals in Canada who are living. If the appellant had had any doubt as to the correctness of this conclusion, he had ample opportunity to cause the facts to be checked and to place evidence with regard thereto before the respondent or the Court. He has not done that and I can only conclude, as the respondent did, that the balance of probability is that there are individuals in Canada whose surname is "FIOR".

With reference to the contention that "FIOR" is not a word, which was the appellant's main contention before the respondent, I have some sympathy with the respondent who did not seem to recognize sufficient merit in the argument to warrant the giving of reasons for rejecting it. The generic definition of "word" in the Shorter Oxford English Dictionary is "Speech, utterance, verbal expression".

The expression "FIOR" may not have any meaning to the general public of Canada as yet but, as far as those who know a person whose surname is "FIOR" are concerned, it means that such a person, and, if this appeal succeeds and the appellant's proposed trade mark becomes an active trade mark, it will operate to distinguish the appellant's goods from the goods of others. For trade mark purposes, there are at least three classes of "words", *viz*, dictionary words, names, and invented words. They are all words, in my view, at least for the purposes of the *Trade Marks Act*. Any other view results in limitations on the application of section 12(1)(*a*) that I cannot think that Parliament intended. I, therefore, reject the contention that "FIOR" is not a "word" within the meaning of that word in section 12(1)(*a*) of the *Trade Marks Act*.

That brings me to the position that I am satisfied that, on the evidence before the respondent and the evidence before me, "FIOR" is "a word that is ... the surname of an individual who is living". The further question to be decided is, whether "FIOR" is "primarily merely" such a word.

In considering this question, it has to be noted that, while it was not established before the respondent by evidence,[4] it was established by affidavit in this Court that "the said trade mark 'FIOR' was created by combining the first letters of each of the words 'fluid iron ore reduction'." As far as the appellant was concerned, therefore, "FIOR" was a word invented by it for use as its trade mark in this connection. It follows, therefore, that "FIOR" is not "merely" the surname of a living person because it also has existence as a word invented by the appellant or persons working for it for trade mark purposes. (It does not appear that the appellant caused the respondent to address his mind to this as an alternative character of the word that ought to be considered in determining whether "FIOR" falls within the words of section 12(1)(*a*).)

The next stage in considering the problem of applying section 12(1)(*a*) to the word "FIOR" is to consider whether "FIOR" is "primarily" the surname of a living person (Note that the French version uses the word "principale-

[4] It had been asserted, but the respondent does not indicate that he saw any relevance to it.

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ment" where the English version uses "primarily".) In other words, is the chief, main or principal character of "FIOR" that of a surname or is it principally or equally a word invented to be used as a trade mark?

Certainly, from the point of view of the people called "Fior" and their immediate circle of friends and acquaintances, the answer is that "Fior" is principally if not exclusively a surname, and from the point of view of the trade mark advisers of the appellant, the answer is that it is principally if not merely an invented word. The test, for the purposes of section 12(1)(*a*) is not, in my view, the reaction of either of these classes of persons. The test must be what, in the opinion of the respondent or the Court, as the case may be, would be the response of the general public of Canada to the word. My conclusion is that a person in Canada of ordinary intelligence and of ordinary education in English or French would be just as likely,[5] if not more likely, to respond to the word by thinking of it as a brand or mark of some business as to respond to it by thinking of some family of people (that is, by thinking of it as being the surname of one or more individuals).[6] Indeed, I doubt very much whether such a

[5] If the two characters (surname and invented word) are of equal importance, it cannot be said that it is "primarily merely" a surname.

[6] I have, in effect, adapted the approach taken by Kekewich J. in *In re The Magnolia Metal Company's Trade Marks,* (1897) 14 R.P.C. 265, where he deals with a similar problem concerning geographical names at pages 269-70, as follows:

> Those being the words of the Act, and that being the object, am I bound to say that the Legislature meant that wherever a name proposed to be put on the Register, or being actually there and sought to be expunged, has a geographical meaning, therefore it must not go on the Register, or, being there, it must be taken off, even though its primary meaning may be something quite different, and it may have two or three other meanings, perhaps all of them better known than the geographical meaning? That is, the real question in this case is the question which was illustrated by some remarks made by myself in the *Apollinaris Company's* case, and which have been cited on page 204 of 1891, 2 Chancery. There, taking up, I suppose, what was said in argument, I instanced or illustrated what I had to say by reference to "Monkey" as connected with soap, and to "St. Paul" as connected with some other goods, I am not sure what. No ordinary person would jump at the conclusion, when he found that soap was called "Monkey", that it had any connection with the one or two by no means large places, or well known to the public, which are called by the name of "Monkey". He would naturally consider

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person would respond to the word by thinking of there being an individual having it as a surname at all.

I am, therefore, of the view that it is probably not "primarily" a word that is a surname of an individual at all, but it is certainly not primarily "merely" such a word.

I have probably been influenced in coming to the conclusion that I have expressed as to how the word "primarily" in section 12(1)(*a*) should be applied by the fact that applying the provision solely by reference to the existence of a dictionary meaning of a proposed trade mark would make practically every invented word vulnerable to attack as a proposed trade mark by anyone assiduous enough to pursue his searches for its use as a surname somewhere in

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that it was connected with the inferior animal of that name. Again, as regards "St. Paul", no one would suppose, if he came across "St. Paul", that any reference was meant other than one to the Apostle known by that name. Nevertheless, it may be (and it appears that it is so) that both are geographical names. Of course, if that had been decided in that case, I should not have been discussing it now, but nothing was decided It seems to me that on these lines I have good ground for consideration whether "Magnolia" here is a geographical name in the sense of its being the primary meaning of the word, or that which would occur to the man of ordinary education and intelligence I must not forget that when I talk of ordinary education and intelligence, I must mean the Englishman of that character. I am not, for a moment, putting out of sight that "geographical" extends to the whole of the world, and that if there is a geographical name derived from any part of the globe, it will offend against the words of the Act; but still, the persons who are to decide, whether it be a judge or a jury, if there is any question for decision at all, must be Englishmen of ordinary education and intelligence. If there is no question to decide, it is because all that you have got to do is to establish, as has been established here, that there are several places known as "Magnolia" in the United States, and that therefore it is in one sense a geographical name, and there is an end of the whole discussion. If there is any question at all, then I think it has to be submitted to the Englishman of ordinary education and intelligence and he has to decide whether that is, I will not say even the primary meaning of the word, but the meaning which would occur to the large majority of people as that which it would be regarded in ordinary society as bearing. Without going into the evidence, I venture to say that a very small proportion of persons of the character I have mentioned would recognise in the word "Magnolia" any reference to any town or place in the United States or elsewhere. On the other hand, though not so common as many other flowers, the magnolia is thoroughly well known to all persons of the character I have mentioned, and if "Magnolia" were mentioned in any ordinary society consisting of persons of fair education, it would be understood at once

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the world (or, indeed, in a country such as Canada even if the search were restricted to Canada). I cannot believe that section 12(1)(*a*) was intended virtually to eliminate the creation of new words for purposes of proposed trade marks.

> to refer to the flower, or the tree which bears that flower. That seems to me to be, I will not say the primary meaning, because primary or secondary are rather out of the question, but the meaning which the word would bear ordinarily to ordinary people. Is there any reason why I should not construe the Act in that way? I admit, and I do not hesitate to say it, I am perplexed by the extreme terseness and literal use of the words "geographical name"; but, on the other hand, I do not think I am bound to decide that it was meant by the Legislature that every word that was capable of being treated as a geographical name, but was also capable of being used, and ought to have been used, among ordinary people as meaning something else, was intended to be referred to as a geographical name.

This case was dealt with by the Court of Appeal in the same volume at page 621 where Rigby L.J., delivering the judgment of the Court, said, at pages 627-8:

> The objection to the word "Magnolia" as being a geographical name within the meaning of the section, in our opinion, fails as to both the marks Nos. 2 and 3. It is, no doubt, shown by the evidence, that there are places in the United States called by the name "Magnolia", and if "geographical name" in Section 64, Subsection (*e*), were equivalent to the name of any place, "Magnolia", as the name of places mentioned in the evidence, would fall within the exception. But, in our judgment, the phrase "geographical name" in Section 64, Sub-section (*e*), ought not in general to receive so wide an interpretation. It must, we think, in the absence of special circumstances, be interpreted so as to be in accordance, in some degree, with the general and popular meaning of the words, and a word does not become a geographical name simply because some place upon the earth's surface has been called by it. For example, we agree with Mr. Justice Kekewich that the word "Monkey" is not proved to be a geographical name, by showing merely that a small and by no means generally-known island has been called by that name.

BETWEEN:

HOME JUICE COMPANY, HOME JUICE COMPANY LIMITED *et al* APPLICANTS;

Ottawa 1968

June 13

June 14

AND

ORANGE MAISON LIMITÉE ....RESPONDENT.

Costs—Summary application to expunge trade mark—Party and party costs—Review of taxation—Negotiations between counsel—Preparation for trial—Tariff A, items 8, 36A—Recommended practice.

REVIEW OF TAXATION.

J. A. Devenny for applicants.

Brian A. Crane for respondent.

JACKETT P.:—This is an application for review of the taxation of the respondent's party and party costs herein.

This proceeding was originated by way of an Originating Notice under section 56 of the *Trade Marks Act* for an order expunging the registration of a trade mark. In accordance with section 58, the application was heard and determined summarily on affidavit evidence and judgment was in due course delivered, dismissing the motion with costs.

The respondent thereupon put before the taxing officer for taxation a bill of costs, claiming a total amount of $4,799.39. This bill was taxed at $1,653.50.

The application for review of the taxation is made under Rule 263 of the Rules of this Court which provides that costs shall be taxed by the Registrar or his deputy "subject, however, to review by the Court".

The Court is asked to review the taxing officer's allowances in respect of two items which read as follows:

8	Preparation for Trial (105 hours × $30 00)	$3,150 00
36A	Negotiation with Christopher Robinson to agree on arrangements to shorten trial (½ day)	200 00

The latter item was claimed and allowed under Item 36A of Tariff A, which reads as follows:

36A. Counsel fees on negotiations with the opposing party with a view to agreeing on facts for purposes of trial or with a view, otherwise, to agreeing on arrangements to shorten or facilitate the trial of the matter, to be allowed on the same basis as counsel fees at trial.

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This item was designed for a case where a trial of an action might take some time and where counsel who are to conduct the hearing have taken steps, other than merely routine steps, with a view to making some special arrangement, such as arriving at an agreement as to facts, whereby the trial might be conducted more expeditiously and more efficiently. In this case I am told that there were a number of telephone conversations between junior counsel for the respondent and counsel for the applicant concerning arrangements for the attendance at the hearing for purposes of cross-examination of persons who had sworn affidavits constituting part of the respondent's material. In my view, no allowance should have been made under Item 36A in this case.

The taxing officer allowed a net amount of $600 in respect of the claim for $3,150 for preparation. This allowance was made under Item 8 of Tariff A, which reads:

> 8. Preparation for trial, including notice of trial, notices to produce and admit, inspections, subpoenas, etc. 30 00
> (Subject to increase in the discretion of the taxing officer)

I find it hard to believe that, in the absence of very special circumstances, of which there are no indications here, any allowance should ever have been made on a party and party taxation in connection with a summary application, for preparation for the hearing, of more than $150. This amount will, therefore, be reduced to $150.

I cannot part from the matter without expressing my apprehension at the way in which party and party costs have apparently tended to grow in magnitude. When the rule of court provides for an item of $30, subject to a discretionary increase, and the party feels justified in claiming over $3,000 and the taxing officer feels justified in increasing the amount of $30, in the case of a one-day hearing, to $600, it somehow seems to me that things have gotten out of proportion.

I should have thought that a bill of over $1,600 is about three times as much as a party and party bill of costs for a summary application such as this should be. I note, for example, that allowance was made in respect of both senior and junior counsel fees. I have difficulty in believing that a proceeding of this kind warranted fees for both leading and junior counsel on a party and party taxation. After discussing the matter with him, I am satisfied that, had an application been made to the Judge who heard the application to fix a lump sum in lieu of taxed costs under Rule 261, it is improbable that he would have fixed more than $500. I myself doubt whether any matter of this kind should ever result in party and party costs exceeding that amount.

I suggest that the presiding Judge should, in the future, entertain any application made at the time of pronouncing judgment to fix a lump sum in lieu of taxed costs in all relatively simple proceedings such as this one.

The taxation is therefore revised and the amount thereof is reduced by $650 to $1,003.50. The matter is returned to the taxing officer to recertify the Bill of Costs accordingly.

Toronto 1968
May 22-24 27, 28
Ottawa June 19

BETWEEN:

SARCO CANADA LIMITED ....APPLICANT;

AND

SARCO COMPANY INC. ....RESPONDENT.

Trade Marks—Trade Marks Act, S. of C. 1952-53, c. 49, ss. 2(t), 18(1)(b), 56(1)—Use of trade mark lost its distinctiveness—Expunging of such trade mark—Invalidity.

On the application by the Canadian company for an order pursuant to section 56(1) of the *Trade Marks Act* to expunge the trade mark "Sarco" of the U.S. company, the evidence was that both companies, during the period 1948 to 1964, did exercise such "equal rights" and used the trade mark "Sarco" in Canada on each of their respective products.

Held, that because of such use this trade mark has lost its distinctiveness;

2. that an order will go expunging the registration of the trade mark "Sarco";

3. that the applicant is entitled to its costs.

APPLICATION to amend registered trade mark.

A. S. Pattillo, Q.C., John W. B. Brown and *G. R. W. Gale* for applicant.

Harold G. Fox, Q.C. and *Donald F. Sim, Q.C.* for respondent.

GIBSON J.:—This is a hearing on the application of Sarco Canada Limited (herein called "Sarco Canada") for an Order pursuant to section 56(1) of the *Trade Marks Act,* 1968 SARCO CANADA LIMITED v. SARCO COMPANY INC. Gibson J.

1953 Statutes of Canada, chapter 49, that the entry in the Register of Trade Marks recorded as Registration No. N.S. 4/1582 in the name of Sarco Company, Inc. (herein called "Sarco U.S.") in respect of the trade mark "Sarco" to be amended by substituting as the owner of the said trade mark the applicant Sarco Canada or alternatively, for an Order expunging the said Registration from the Register.

The date of this application was February 26, 1964.

The applicant (herein sometimes referred to as Sarco Canada) was incorporated under the laws of the Province of Ontario by Letters Patent dated July 8, 1929. The principal objects are "to manufacture, buy and sell 'Sarco products', steam traps, radiator traps, valves and temperature control and industrial equipment of all kinds". The applicant at that time was a wholly-owned subsidiary of the respondent in these proceedings (herein sometimes referred to as Sarco U.S.) a company incorporated under the laws of one of the States of the United States of America. Sarco U.S. executed at that time a Consent to the incorporation of Sarco Canada and the use by it of the corporate name "Sarco (Canada) Limited".

From 1908 to 1929 Sarco U.S. sold its products in Canada through an agent by the name of Peacock Bros.

From 1929 until 1941 Sarco U.S. products were sold in Canada through Sarco Canada.

In 1941 Sarco Canada began to manufacture certain Sarco products pursuant to the specifications of Sarco U.S. and began to also sell these products along with Sarco U.S. products.

By 1948 Sarco Canada manufactured approximately 45% of all the products sold by it in Canada and about 21% of the products sold were those of Sarco U.S. The balance of products Sarco Canada sold in Canada were products purchased from other manufacturers.

The chief shareholder of Sarco U.S. and Sarco Canada until 1948 was one H. Clement Wells. He also owned the majority of shares in an English Sarco business carried on by Spirax-Sarco Engineering Limited and a number of foreign companies by the control exercised through a company called Sarco International Corporation, examples of which were Sarco Belge S.A. (Belgium), Sarco G.M.B.H. (Germany) and Inde E. Com. Sarco Sud Americana Ltds. (Brazil).

In 1948 H. Clement Wells for the welfare of his brother Eric E. Wells caused to be transferred from Sarco U.S. to Eric E. Wells all the shares of Sarco Canada which in turn were transferred by Eric E. Wells to trustees upon certain trusts *inter alia* and speaking generally, to provide a pension to Eric E. Wells for his life and after his death, to his widow, after which the shares were to be held by trustees for the benefit of the employees of Sarco Canada.

From this time in 1948 until the date of this application, Sarco Canada ceased to be a U.S. subsidiary to Sarco U.S. and was an independent company.

But from 1948 to 1964 the date of this application, Sarco Canada sold Sarco U.S. products as above mentioned.

In 1933 an application was made to the Registrar of Trade Marks on behalf of Sarco U.S. for the registration of the trade mark "Sarco" as a word mark and the trade mark "Sarco" in respect of the wares "steam traps, thermostats, strainers, steam valves and fittings" was registered on August 29, 1933 as No. 1582 Folio 4. Renewals of the registration were made by Sarco U.S. as from August 29, 1948 and August 29, 1963.

At no time was there any formal assignment of the trade mark "Sarco" for use in Canada by Sarco U.S. to Sarco Canada, or formal licence to use it.

In the period 1960 to 1964, Sarco U.S. made certain sales of its product directly to Canadian purchasers. In addition, certain of the Sarco U.S. products were sold through Sarco Canada in an unchanged condition both as to labels on the products and on the containers and on the literature of instructions enclosed to Canadian customers.

The applicant's witness A. C. Simpkins, G. Granek and W. H. Evans, who were independent witnesses, knew that Sarco products were made by both Sarco Canada and Sarco U.S. and were sold to Canadian customers. The respondent's witness Francis Winchester who was agent from 1951 to 1964 for Sarco Canada in the Quebec area, said that "Sarco" meant to him, during that period, products of both Sarco U.S. and Sarco Canada.

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There was a free exchange of technical information, know-how and other help between Sarco U.S. and Sarco Canada from 1948 to 1964 without payment of any monies.

Eric E. Wells died in 1958 and H. Clement Wells died in 1964 having retired to Europe in 1955.

Counsel for the applicant submitted (1) that the applicant was not a licensee of Sarco U.S. of the trade name "Sarco", on the day of this application or in the period 1948 to 1964; (2) that the applicant was not an agent of Sarco U.S. during the period 1948 to 1964; (3) that the trade mark "Sarco" during the period 1948 to 1964 was not distinctive in Canada of the wares of Sarco U.S.; (4) that under section 56(1) of the *Trade Marks Act* the name Sarco U.S. should be expunged as owner of the trade mark "Sarco"; and (5) that the Register should be altered to record the name of Sarco Canada as owner because: (i) the trade mark "Sarco" is distinctive of the wares of Sarco Canada; and (ii) that Sarco Canada is the beneficial owner and was the sole user of the mark in Canada during the period 1948 to 1964.

Counsel for the respondent submitted that (1) the applicant is a licensee of the owner of the trade mark and is therefore estopped or otherwise precluded from attacking the validity of the trade mark and its registration and the title of its licensor; (2) (as a corollary of the first submission) that there has existed an agency or "permitted use" situation and the applicant is likewise estopped or otherwise precluded from questioning validity and title; (3) the trade mark is and always has been distinctive in Canada of the goods of the respondent, Sarco U.S.; (4) if these submissions are not accepted, that the respondent has no defence to the claim for expungment; and (5) that the Register should not be amended to show Sarco Canada as owner of the trade mark because at no time was the trade mark "Sarco" ever distinctive of the wares of Sarco Canada in Canada.

On the whole of the evidence, it is clear that H. Clement Wells (who as stated, at one time for all practical purposes, was the sole owner of the shares of all the Sarco Company throughout the world) at the material time in 1948 was the sole owner of Sarco U.S. which latter Company in turn owned all the shares of Sarco Canada. He wished to look after the welfare of his brother Eric E. Wells and his wife and also the employees of Sarco Canada. That is the reason he entered into the 1948 transaction. It also explains the relationship between Sarco U.S. and Sarco Canada during the period 1948 on and until the time both he and Eric E. Wells ceased to be connected with either Company, and until these companies became controlled by strangers to the Wells brothers and to each other.

As a result, when H. Clement Wells and Eric E. Wells were respectively associated with these two Companies as between the two Companies, no one paid much attention to the method of the use of the Canadian registered trade mark "Sarco". It was used indiscriminately on both the products of Sarco U.S. and the products of Sarco Canada which were sold in Canada.

In support of their respective contentions as to whether the basis upon which Sarco Canada used the trade mark "Sarco" was one of implied licence or agency counsel for each of the parties submitted that there is an issue of credibility as between the evidence of their respective witnesses.

Such issue, counsel contended, extended also to the submission as to whether or not there was an assignment in equity of the trade mark "Sarco" to Sarco Canada in 1948.

The issue of credibility does not, however, extend to the question of distinctiveness. All witnesses say in effect that to each of them they associated the trade mark "Sarco" with the wares of both Sarco U.S. and Sarco Canada.

On the issue of implied licence or agency, certain of the evidence contained in the affidavit of Herbert L. Simmons filed by the respondent is conclusive in my view.

In this evidence Mr. Simmons says he was first employed by Sarco U.S. as office manager in 1925; that from that time until 1955 when Mr. H. Clement Wells was practically 82 years, he was intimately associated with him; that he was credit manager of Sarco U.S. in 1933, office manager and assistant treasurer in 1945 and director of Sarco U.S. in 1948 and was designated by H. Clement Wells to succeed him as President and Treasurer of Sarco U.S. on January 1, 1955; that for many years he was an officer and director of other Sarco Companies; that in the 1930's he was Mr. H. Clement Wells' "right-hand man and confidential assistant" in the management of all the Sarco

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Companies wherever located and that therefore "for almost 40 years" he has been an officer of Sarco U.S. and also had an intimate knowledge during that period of "the Sarco Company's operation" and he had "a personal association with Mr. Wells for approximately 20 of those 40 years".

In paragraph 5 of this affidavit evidence Mr. Simmons also says:

> I have never made an agreement either formal or informal—with Sarco Canada Limited regarding the use of the name and mark "Sarco", and have always respected the right of Sarco Canada Limited to use the name "Sarco" which was given to it in 1929 as part of the application for its incorporation. I have always believed that Sarco Company, Inc. and Sarco Canada Limited have equal rights to use the name and mark "Sarco" in Canada ...

From this I find that on true interpretation this means that there was no implied licence to use the trade mark "Sarco" by Sarco Canada and no agency arrangement between Sarco U.S. and Sarco Canada as to its use. This means precisely what it says, *viz* that from 1948 to 1964 Sarco Canada had "equal rights to use the trade name 'Sarco' in Canada". Having such "equal rights" negatives any licence or agency arrangement.

And, on the evidence, I find that during the period 1948 to 1964 both parties did exercise such "equal rights" and used the trade mark "Sarco" in Canada on each of their respective products.

As a result, the trade mark "Sarco" during that period was not solely distinctive either of the wares of Sarco U.S. or of the wares of Sarco Canada.

In other words, during this period this trade mark lost its distinctiveness.

This is one of the statutory grounds of invalidity. (See *Trade Marks Act* section 18(1)(*b*) which reads:

> 18. (1) The registration of a trade mark is invalid if
>
> . . .
>
> (*b*) the trade mark is not distinctive at the time proceedings bringing the validity of the registration into question are commenced;)

By definition, a trade mark must be distinctive of only one person's wares. (See *Trade Marks Act* section 2(*t*)) which reads:

> (*t*) "trade mark" means
>
> (i) a mark that is used by a person for the purpose of distinguishing or so as to distinguish wares or services

manufactured, sold, leased, hired or performed by him from those manufactured, sold, leased, hired or performed by others,

(ii) a certification mark,

(iii) a distinguishing guise, or

(iv) a proposed trade mark;)

"Distinctive" is defined in section 2(*f*) of the *Trade Marks Act* as follows:

> (*f*) "distinctive" in relation to a trade mark means a trade mark that actually distinguishes the wares or services in association with which it is used by its owner from the wares or services of others or is adapted so to distinguish them;)

In *Western Clock Company v. Oris Watch Company, Ltd.*[1] Audette J. said:

> Distinctiveness is of the very essence and is the cardinal requirement of a trade-mark, which is used to distinguish the goods of a trader from the goods of all other traders.

In *C. Fairall Fisher et al v. British Columbia Packers Limited*[2] Thorson P. said:

> ...It is clear from these definitions that distinctiveness is an essential requirement of a trade mark.

In *Standard Ideal Company v. Standard Sanitary Manufacturing Company*[3] Lord MacNaghten said:

> ...Distinctiveness is the very essence of a Trade Mark.

The decision on this application therefore is that because this trade mark has lost its distinctiveness that an order will go that the entry in the Register of Trade Marks recorded as Registration No. N.S. 4/1582 in the name of Sarco Company, Inc. in respect of the trade mark "Sarco" be expunged.

The applicant is entitled to its costs.

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[1] [1931] Ex. C.R 64 at 67.

[2] [1945] Ex. C.R. 128 at 132.

[3] (1910) 27 R P C 789 at 796

Saint John 1968

June 4

Ottawa June 20

BETWEEN:

DAVID S. CHRISTIE, Executor of the Estate of Charles S. Christie ...... APPELLANT;

AND

THE MINISTER OF NATIONAL REVENUE .... RESPONDENT.

Estate tax—Wife predeceasing husband—Wife entitled to interest in expectancy in father's estate—Death of husband before wife's estate administered—Valuation of husband's interest in wife's estate—Estate Tax Act, R.S.C. 1958, c. 29, s. 58(1)(o), s. 58(1)(s)(i) and (ii).

Mrs. C, who was residuary legatee of her father's estate expectant on the death of her mother as life tenant, died intestate in 1963 survived by her husband and son, who were entitled to share her estate equally by the laws of New Brunswick, where she and her husband were domiciled. The husband, who died soon afterward, bequeathed his estate to the son, who obtained administration of both estates. In assessing the husband's estate the Minister included his half interest in his wife's estate, valuing it at $52,579 under s. 58(1)(*s*)(i) of the *Estate Tax Act*.

Held, confirming the assessment, on the death intestate of the wife the husband acquired a right to have her estate administered, which is a chose in action and therefore "property" within the definition of s. 58(1)(*o*); that right's value was the value of the husband's half interest in his wife's interest in expectancy in her father's estate computed under s 58(1)(*s*)(i), and not merely the value of his right to have her estate administered computed at its fair market value under s. 58(1)(*s*)(ii)—as to which there was no evidence in any event. *Lord Sudeley v. Att'y-Gen.* [1897] A C. 11, applied.

APPEAL under *Estate Tax Act.*

Ian M. Whitcomb for appellant.

M. A. Mogan for respondent.

CATTANACH J.:—This is an appeal under the *Estate Tax Act* from an assessment in respect of the estate of Charles S. Christie, who died testate at the City of Saint John, in the Province of New Brunswick on August 10, 1964, by his son, David S. Christie as executor.

Immediately prior to trial the parties agreed upon an admitted statement of facts in the following terms:

> The Appellant and the Respondent hereby admit the several facts respectively hereunder specified but these admissions are made for the purpose of this appeal only and may not be used against either party on any other occasion or by any other than the Appellant and the Respondent. The parties reserve the right to object

to the admissibility of any or all of the said facts on the ground that they are not relevant or material to any of the issues to be determined in this appeal.

1. Charles S. Christie (hereinafter called for reasons that will later become apparent "the second decedent") died testate, resident and domiciled in the Province of New Brunswick on August 10, 1964.

2 On February 7, 1964, the second decedent signed, published and declared his last will and testament wherein, inter alia, he nominated his only son, the Appellant, his sole executor and residual beneficiary.

3. The second decedent's estate was admitted to probate in the Probate Court, County of Kings, Province of New Brunswick, on September 18, 1964. Administration of the estate was granted to the Appellant in accordance with the second decedent's last will and testament.

4. The second decedent was predeceased by his wife, Mary Louise Christie (hereinafter called "the first decedent") who died intestate, resident and domiciled in the Province of New Brunswick on October 31, 1963.

5. The first decedent's estate was originally admitted to probate in the Probate Court, County of Kings, Province of New Brunswick, on September 18, 1964, being the same date on which the second decedent's estate was so admitted. Administration of the first decedent's estate was granted to the Appellant.

6. The Appellant, as administrator of the first decedent's estate, filed an ET60 Estate Tax Return dated November 12, 1964, wherein he reported the property of the first decedent as having a total value of $57,807 70.

7. By Notice of Assessment dated the 18th day of March, 1966, the Respondent increased the reported total value of the property of the first decedent by the sum of $58,975.74 to produce, for assessing purposes, a revised total value in the amount of $116,063 44; and a revised aggregate net value in the amount of $115,500.94.

8. Annexed hereto as Exhibit "A" is a photocopy of the Notice of Assessment of the first decedent's estate dated the 18th day of March, 1966, to which is annexed photocopies of Forms ET86A, ET85 and an unnumbered form dated the 28th day of February, 1966, with the initials GR/GHP.

9. By a Notice of Re-Assessment dated the 5th day of October, 1967, the Respondent decreased the revised total value of the property of the first decedent (as determined by the assessment of March 18, 1966—Exhibit "A") by the sum of $2,704 24 to produce, for assessing purposes, a revised total value in the amount of $113,359.20; and a revised aggregate net value in the amount of $112,796.70.

10. Annexed hereto as Exhibit "B" is a photocopy of the Notice of Re-Assessment of the first decedent's estate dated the 5th day of October, 1967, to which is annexed photocopies of Forms ET86A, ET85 and an unnumbered form dated the 20th day of September, 1967, with the initials GKR/AMO'P.

11. The Appellant, as administrator of the first decedent's estate, did not object to or appeal from the said Re-Assessment (Exhibit "B") of October 5, 1967.

12. The Appellant, as executor of the second decedent's estate, filed an ET60 Estate Tax Return dated November 17, 1964, wherein

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he reported the property of the second decedent as having a total value of $152,432.24. In computing the said total value, the Appellant included the sum of $31,029.59 as representing the second decedent's interest in the estate of the first decedent.

13. By Notice of Assessment dated the 17th day of March, 1966, the Respondent increased the reported total value of the property of the second decedent by the sum of $106,831.02 to produce, for assessing purposes, a revised total value in the amount of $259,263 26.

14. In the said sum of $106,831 02, the Respondent included the amount of $18,209 85 representing an increase in the value of the second decedent's interest in the estate of the first decedent from $31,029.59 (as reported) to $49,239.44.

15. Annexed hereto as Exhibit "C" is a photocopy of the Notice of Assessment of the second decedent's estate dated the 17th day of March, 1966, to which is annexed photocopies of Forms ET86A, ET85 and an unnumbered form dated the 1st day of March, 1966, with the initials GKR:ADK.

16. By Notice of Objection dated the 13th day of June, 1966, the Appellant objected to the Assessment (Exhibit "C") of the second decedent's estate.

17 By a Notice of Re-Assessment dated the 5th day of October, 1967, the Respondent increased the revised total value of the property of the second decedent (as determined by the Assessment of March 17, 1966) by the sum of $3,340.40 to produce, for assessing purposes, a revised total value in the amount of $262,603 66.

18. The said sum of $3,340 40 represented an increase in the value of the second decedent's interest in the estate of the first decedent from $49,239 44 (as determined by the previous Assessment—Exhibit "C") to $52,579.84.

19. Annexed hereto as Exhibit "D" is a photocopy of the Notice of Re-Assessment of the second decedent's estate dated the 5th day of October, 1967, to which is annexed photocopies of Forms ET86A, ET85 and an unnumbered form dated the 20th day of September, 1967, with the initials GKR/AMO*P.

20 In this Agreed Statement of Facts, the parties have used the phrase "the second decedent's interest in the estate of the first decedent" as a matter of convenience, and this phrase is not to be taken as an admission by the Appellant that the second decedent did in fact have an interest in the estate of the first decedent.

THE PARTIES HERETO reserve the right to call such further and other evidence as Counsel may advise

Appended to the Agreed Statement of Facts were Exhibits A, B, C, & D.

Exhibit "A" is comprised of a Notice of Assessment of Mrs. Christie's estate, Department of National Revenue forms ET86A and ET85 showing the calculation of tax and valuation charges and a further sheet showing the calculation of the interest in expectancy in the estate of Otty J. Fraser. Exhibit "A" is referred to in paragraphs 8 and 9 of the Agreed Statement of Facts.

Exhibit "B" is comprised of a revised Notice of Assessment of Mrs. Christie's estate, forms ET86A and ET85, being a calculation of the revised tax and valuation charges and a revised computation of the interest in expectancy in the estate of Otty J. Fraser. Exhibit "B" is referred to in paragraphs 10 and 11 of the Agreed Statement of Facts.

Exhibit "C" is comprised of a Notice of Assessment of Mr. Christie's Estate, forms ET86A, being the calculation of tax and ET85, being valuation charges, as well as a sheet calculating the value of Mr. Christie's interest in his wife's estate and a further calculation of the value of the expectancy of Mrs. Christie in her father's estate as at the date of Mr. Christie's death. Exhibit "C" is referred to in paragraphs 15, 16 and 18 of the Agreed Statement of Facts.

Exhibit "D", which is referred to in paragraph 19 of the Agreed Statement of Facts, is a revised Notice of Assessment of the estate of Mr. Christie, with supporting documents as in the previous exhibits.

Neither party called any further evidence in accordance with the reserved right to do so in the concluding paragraph of the Agreed Statement of Facts.

The facts so outlined may be stated briefly. Mrs. Christie died intestate on October 31, 1963. The aggregate net value of her estate was computed by the Minister to have been $112,796.70 for assessment purposes. Included in these assets was the value of Mrs. Christie's interest in expectancy in the estate of her father, Otty J. Fraser, as at October 31, 1963, computed by the Minister to have been in the amount of $106,919.53. In his will, the late Otty J. Fraser, after making certain specific bequests had directed the payment of the income from the residue of his estate to his wife during her lifetime, with authority to the trustees to encroach on the corpus of his estate if necessary for that purpose. On the decease of his wife he had then bequeathed the residue of his estate to his daughter, Mrs. Christie, to be hers absolutely. Both parties agreed and the present issue was argued upon the basis that the interest in expectancy of Mrs. Christie in her father's estate constituted part of her estate passing on her intestacy. The assessment of Mrs. Christie's estate was neither objected to nor appealed.

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By virtue of the provisions of the *Devolution of Estates Act*[1] applicable to intestate succession, Mrs. Christie's estate was divisible in equal shares between the appellant herein as her only child and Charles S. Christie as her husband.

Mr. Christie died testate on August 10, 1964, 284 days after the death of his wife, prior to the grant of administration of Mrs. Christie's estate. In fact the administration of the estates of Mrs. Christie and Mr. Christie was granted on the same day, September 18, 1964, to the appellant herein, David S. Christie, their only son and issue.

In assessing the estate of Charles S. Christie as he did, the Minister computed the total value for assessment purposes at an amount of $262,603.66 included in which was the value of a one-half interest in the estate of his wife, in the amount of $52,579.84. It is to the inclusion of this amount and to the valuation of the interest to Mr. Christie in the estate of Mrs. Christie that the appellant objects. The appellant does not object to the accuracy of the Minister's mechanical computation, nor to the figures used therein, but he says that the Minister based his computation upon incorrect principles.

As I understood the argument on behalf of the appellant, it was that at the time of Mr. Christie's death his only right or interest in the estate of his wife was that of a next-of-kin or heir-at-law in the unadministered estate of a deceased person; that such right was a chose in action consisting solely of a right to have the estate of his wife properly administered; that such chose in action was not an "income right, annuity, terms of years, life or other similar estate or interest expectancy" within the meaning of these words in section 58(1)(*s*)(i) of the *Estate Tax Act* and accordingly the method of valuation, as prescribed by the regulations referred to in such sub-section, is not applicable but rather that the value of such chose in action should be the fair market value within section 58(1)(*s*)(ii) and that such value is nil or at least negligible.

Section 58(1)(*s*) reads as follows:

(1) In this Act,

(*s*) "value",

(i) in relation to any income right, annuity, term of years, life or other similar estate or interest in expectancy,

[1] R.S.N.B. 1952, c. 62.

means the fair market value thereof ascertained by such means and in accordance with such rules and standards, including standards as to mortality and interest, as are prescribed by the regulations, and

(ii) in relation to any other property, means the fair market value of such property,

computed in each case as of the date of the death of the deceased in respect of whose death such value is relevant or as of such other date as is specified in this Act, without regard to any increase or decrease in such value after that date for any reason.

An "interest in expectancy" is defined in section 58(1)(*k*) as including "an estate or interest in remainder or reversion and any other future interest whether vested or contingent, but does not include a reversion expectant on the determination of a lease".

The fair market value of an interest in expectancy is to be ascertained in accordance with formula outlined in section 10 of the Estate Tax Regulations.

There is no doubt whatsoever in my mind that the interest which Mrs. Christie had in the estate of her father as remainderman subject to the life interest of her mother was an "interest in expectancy" within the meaning of those words as they appear in section 58(1)(*s*)(i) of the *Estate Tax Act* and as those words are defined in section 58(1)(*k*) and that accordingly the Minister's valuation of that interest for the purpose of assessment of Mrs. Christie's estate was properly computable in accordance with the Regulations.

The question for determination in the present appeal is whether Mrs. Christie died possessed of any property which passed upon her death to her husband and if so what was the value of that property. Was it valueless as contended by the appellant or was it $52,579.84 as computed by the Minister and contended by him to be the correct value?

To arrive at the above figure the Minister computed the increase in the value, because of the further advance in years of Mrs. Christie's mother, of the interest in expectancy which Mrs. Christie had in the estate of her father, as at August 10, 1964, the date of Mr. Christie's death, in accordance with the method outlined in section 58(1)(*s*)(i), and added that increase to the value of Mrs. Christie's interest in expectancy which had been computed by the same formula as of October 31, 1963, the date of

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Mrs. Christie's death and divided the result by two. This computation is set forth on the fourth page of Exhibit "D" to the Agreed Statement of Facts. As I have intimated above, there is no dispute as to the accuracy of the computation, but the dispute is as to whether such method of computation is properly applicable in the facts of this appeal.

The first step in the contention of the appellant, as I understood it, was that no property passed on the death of Mrs. Christie to her husband.

Section 3(1) of the *Estate Tax Act* reads in part,

> 3. (1) There shall be included in computing the aggregate net value of the property passing on the death of a person the value of all property, wherever situated, passing on the death of such person, . . .

The appellant contended that all that passed to Mr. Christie was a right to have the estate of Mrs. Christie administered which is not a proprietary interest but merely a "nebulous" interest.

The right that passed to Mr. Christie is a right properly enforceable by legal action and was accordingly a chose in action, a premise which was accepted by counsel for both parties and with which I am also in agreement.

In section 58(1)(*o*) of the *Estate Tax Act* property is defined as meaning "property of every description whatever, whether real or personal, movable or immovable, or corporeal or incorporeal, and without restricting the generality of the foregoing, includes any estate or interest in any such property, a right of any kind whatever and a chose in action;".

In view of the express terms of the foregoing definition, I cannot accede to the appellant's submission that no property passed on the death of Mrs. Christie to her husband.

The next problem is to ascertain if the value of the property so passing was properly determined.

The Minister's contention is that it is not the value of Mr. Christie's right to have his wife's estate administered which should be included in the aggregate net value, but the value of the assets which will devolve upon him as a consequence of that right.

What Mrs. Christie had, among other assets of lesser value, was an interest in expectancy in the estate of her father. Upon her intestacy her husband was given a statutory right by virtue of the *Devolution of Estates Act* (*supra*) to participate to the extent of one-half in the distribution of that asset. It would seem to me that what Mr. Christie could expect to receive upon the distribution of his wife's estate was a one-half interest in his wife's interest in expectancy and accordingly I cannot follow how that asset can be anything other than an interest in expectancy for which the value is to be computed in accordance with section 58(1)(*s*)(i). The Minister so computed the value of that asset at the time of Mr. Christie's death and in my opinion, he was right in doing so.

In *Lord Sudeley and Others v. The Attorney-General (on behalf of Her Majesty)*[2], the House of Lords affirmed the majority decision of the Court of Appeal[3]. In that case the executors of Frances Tollemache were entitled to a fourth part of the residuary estate of her late husband. Mrs. Tollemache and her late husband had been domiciled and had died in England. A sum of £111,850, part of such residuary estate, was the value of one-fourth part of mortgages in New Zealand. The Crown claimed probate duty on this sum. The executors resisted the claim on the ground that the sum was the value of a foreign and not an English asset and was, therefore, not subject to probate duty in England. It was held that such sum was an English asset. The only interest that the executors of Frances had in the estate of her husband was the right to recover from her husband's executors one-fourth of the clear residue of his estate. This was held to have been a chose in action situated in England. Therefore probate duty was held to have been payable upon such asset. However the value of the asset, i.e. English chose in action, being the right of Frances to have her husband's estate administered, was held to have been one-fourth of the value of the New Zealand mortgages by Lopes and Kay L.JJ. in the Court of Appeal (Lord Esher M.R. dissenting). The House of Lords agreed with the majority in the Court of Appeal. Therefore the Court of Appeal and the House of Lords placed a value of the chose in action for probate duty purposes at the precise value of one-fourth

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2 [1897] A.C. 11.

3 [1896] 1 Q.B. 354.

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part of the New Zealand mortgages, that is the value of the asset which formed the basis of the chose in action. This is what the Minister did in the present instance and, in my view, he was correct in doing so.

Even assuming that the proper valuation of the property should have been the fair market value in accordance with section 58(1)(*s*)(ii), as was contended by the appellant, with which contention I do not agree, there was no evidence adduced before me to support the allegation in Head B, paragraph 2(*d*) of the Notice of Appeal that the "aforementioned chose in action had no exchangeable or fair market value" at the relevant date. Therefore, the appellant has failed to discharge the onus upon him to demonstrate that the assessment by the Minister was wrong.

For the foregoing reasons the appeal is dismissed with costs.

Ottawa
1968
May 13-17, 21-24, 27-29
June 21

BETWEEN:

CLAIROL INTERNATIONAL CORPORATION AND CLAIROL INC. OF CANADA .... PLAINTIFFS;

AND

THOMAS SUPPLY & EQUIPMENT COMPANY LIMITED AND THOMAS PRODUCTS CORPORATION LTD. AND REVLON INC. .... DEFENDANTS.

Trade marks—Use of competitor's trade marks in colour comparison charts—Whether false in material respect and likely to mislead public—Whether contrary to honest industrial or commercial usage—Whether violation of registered owner's exclusive right—Whether likely to depreciate value of goodwill attaching to trade marks—Trade Marks Act, secs. 7(d), 7(e), 19, 22.

Defendants marketed hair colouring products under the trade marks *Revlon* and *Colorsilk*, employing advertising brochures and packages which contained colour comparison charts of defendants' and competitive products in which plaintiffs' products were identified by their registered trade marks *Miss Clairol* and *Hair Color Bath*. The plaintiffs' trade marks were widely advertised and their hair colouring products dominated the market

Held, defendants were not in violation of secs. 7(*d*), 7(*e*) or 19 of the *Trade Marks Act* but were in violation of s. 22, and plaintiffs were entitled to relief including damages

1. Defendants' representations did not falsely describe defendants' products in a material respect and so violate s. 7(*d*) of the *Trade Marks Act*.

2. Defendants' reference to plaintiffs' products was not "contrary to honest industrial or commercial usage in Canada" within the meaning of s. 7(*e*) of the *Trade Marks Act* as being a device for describing defendants' products as equivalent to plaintiffs' and thus to obtain the benefit of the goodwill which plaintiffs had built up over a long period by great effort and massive advertising. In the context of section 7 as a whole para. (*e*) does not prevent a person from taking advantage of a market situation created by the efforts of another if the means used are not dishonest. *Eldon Industries Inc. v. Reliable Toy Co.* (1968) 48 C.P.R. 109, referred to.
3. While defendants' use of plaintiffs' trade marks on the packages, though not in the brochures, was a use of those marks in association with the packaged wares within the meaning of s. 4(1) defendants did not thereby infringe plaintiffs' exclusive right to the use of those marks under s 19, which right, in view of the definitions of "use" and "trade mark" in secs. 2(*v*) and 4, does not apply to use of a trade mark otherwise than to identify the user's wares. *Irving's Yeast-Vite Ltd. v. F. A. Horsenail* (1934) 51 R.P C. 110, referred to.
4. In placing plaintiffs' trade marks on the packages (though not in the brochures) defendants used the marks, in association with their wares within the meaning of s 4 "in a manner likely to have the effect of depreciating the value of the goodwill attaching thereto" within the prohibition of s 22 of the *Trade Marks Act*. (*Trego v. Hunt* [1896] A.C. 7, applied.) The verb "use" in s. 22(1) is to be interpreted by reference to the definition of the noun "use" in s 2(*v*). The goodwill attached to a trade mark is that portion of the goodwill of the business of its owner consisting of the whole advantage, whatever it may be, of the reputation and connection which may have been built up by years of honest work or gained by lavish expenditure of money and which is identified with the goods distributed by the owner in association with the trade mark (*Trego v. Hunt, supra,* referred to) Depreciation of the value of that goodwill occurs whether through reduction of the esteem in which the mark is held or through enticement of customers for goods bearing the mark (though not from loss of exclusive rights as a result of use by others, since that affects the trade mark itself rather than the goodwill attached to it).

ACTION for infringement of trade marks.

Gordon F. Henderson, Q.C. and *Rose-Marie Perry* for plaintiffs.

C. A. Scott, Q.C. and *David W. Scott* for defendants.

THURLOW J.:—In this action the plaintiffs claim an injunction, damages and other relief in respect of the use by the two first named defendants of what are known as color comparison charts which contain *inter alia* the plaintiffs' trade marks and which are endorsed on the packages in which the defendants' goods are sold and are also included in brochures circulated by the defendants in the course of their business of dealing in hair coloring products.

In what follows I shall refer to the first and second named defendants as "the defendants". The defendant, Revlon Inc., was not served in these proceedings and on the matter being raised at the commencement of the trial counsel for the plaintiffs elected to discontinue the action against that defendant rather than have the trial postponed.

The first named plaintiff is a New York corporation and is the owner of the trade mark *Miss Clairol* which is registered in its name for use in association with hair tinting and coloring preparations. The second named plaintiff, is a Canadian corporation and is a subsidiary of the first named plaintiff. It is a registered user of the trade mark *Miss Clairol* and is the owner of the trade mark *Hair Color Bath* which is registered in its name, also for use in association with hair tinting and coloring preparations.

The defendants are Canadian corporations incorporated in or about 1932 and 1958 respectively. The senior corporation, Thomas Supply and Equipment Company Limited, has been engaged since its incorporation in the manufacture and sale of various cosmetic articles and the junior corporation since incorporation has been engaged in the sale and distribution of cosmetic products manufactured by the other. From the times of incorporation both of these corporations were controlled by Christopher Trahern Thomas but in June of 1967 control of the defendant Thomas Products Corporation Ltd. became vested in Revlon Inc., the third named defendant. That defendant from January 1958 until January 1965 was the owner of the trade mark *Revlon* which had been registered in 1932 by the Revlon Nail Enamel Corporation, later named Revlon Products Corporation, for use in association with a number of cosmetic products (not, however, as I read the registration, including hair coloring preparations). In January 1965 ownership of this trade mark was transferred to Revlon (Suisse) S.A. and that corporation in September 1966 secured the registration of the trade mark *Colorsilk* for use in association with hair color preparations. From June 28, 1955, to January 1, 1965, the defendant Thomas Supply and Equipment Company Limited was a registered user of the trade mark *Revlon*. The defendant Thomas Products Corporation Ltd. became a registered user of the same mark on November 28, 1958, and still is a registered user of it. The same defendant became a registered user of the trade mark *Colorsilk* from September 2, 1966, and is still a registered user of it.

The advertising brochures and packages complained of were prepared and used in respect of hair coloring products manufactured by the first named defendant and sold by it to the second named defendant by whom they were sold and distributed to beauty salons and franchised retail dealers such as drug and department stores. The goods in question and the brochures all bore the trade marks *Revlon* and *Colorsilk* pursuant to arrangements between the defendants and Revlon Inc. But the printed matter in the brochures and on the packages also included the color comparison charts in question in which both of the trade marks, *Miss Clairol* and *Hair Color Bath,* also appeared. In each of the two brochures complained of these marks appeared on a page headed *Comparative Shade Chart* and at the head of the second of four columns. In each case the first of the columns was headed *Revlon Colorsilk Hair Color* and contained a list of names of color shades (with numbers) each of which was illustrated elsewhere in the brochure. Under the heading *Miss Clairol Hair Color Bath* appeared a list of numbers which corresponded to numbers used by the plaintiffs to identify their color shades. The other two columns were also lists of numbers used to identify color shades. In the earlier chart they were headed *Helena Rubenstein Tintillate* and *Alberto Culver New Dawn* respectively. In the later chart they were headed *Clairol Nice'n Easy* and *Alberto Culver New Dawn* respectively.

On the packages complained of the marks *Revlon* and COLORSILK appeared prominently on the top and bottom and on all four sides but on one of the sides under the marks *Revlon* COLORSILK were the words:

> SHAMPOOS IN. . .
> WON'T WASH OUT!
> COMPARATIVE HAIR COLOR
> SHADE CHART
>
> The sparkling, natural-looking Revlon Hair Color Shades correspond approximately to the competitive shades indicated:

and this was followed by a chart consisting of two columns the first headed *Revlon* COLORSILK and containing a list

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of names of shades with identifying numbers and the second in smaller type headed *Miss Clairol Hair Color Bath* and containing a list of the plaintiffs' color identification numbers.

The earlier of the two brochures was published in June 1965 when the first of the packages complained of was put on the market. In all 1260 copies of this brochure were distributed in Canada. The other brochure was published in April 1966 after the commencement of the action and 1525 copies of it have been distributed in Canada. In the meantime the plaintiffs' product referred to as *Clairol Nice'n Easy* had appeared on the market and the defendants had put on the market two additional shades of hair color and had altered the wording on the packages by replacing the words SHAMPOOS IN... WON'T WASH OUT! with the words COVERS GRAY . . . LIGHTENS OR DARKENS and by adding references to its new shades in the color comparison chart thereon. It had also added references to its new shades in the new brochure. On a later package introduced in 1968 the number of shades was reduced from 14 to 11 and comparative numbers of the plaintiffs' colors were given for only 5 of them.

The trade mark *Miss Clairol* had been advertised extensively in Canada as well as in the United States in association with the plaintiffs' hair coloring preparations and it is and was admittedly a well known trade mark for such preparations throughout Canada. It was said that in 1965 the plaintiffs enjoyed 50 per cent. of the market for such preparations in the beauty salon trade and 70 per cent. of the market for them in drug, department and other retail stores. Marketing of the plaintiffs' preparations was carried out through jobbers and the goods found their way into whatever salons and retail outlets wished to carry them.

The trade mark *Revlon* is and was admittedly also a well known trade mark throughout Canada for a line of cosmetic products, it too having been extensively advertised in Canada as well as in the United States. There is, however, no evidence that it was a well known trade mark in respect of hair coloring preparations prior to June of 1965 when the events complained of began.

It was said that the market for hair coloring preparations has been growing at the rate of about 15 per cent. per year and there is evidence that the plaintiffs' sales of the products marketed in association with the trade mark *Miss Clairol* increased in each of the years 1963 to 1967 over the previous year except that in 1965 they decreased by $100,-000. It was in June of 1965 that the defendants' hair coloring preparation was put on the market but in the same year the plaintiffs also put on the market the product known as *Clairol Nice'n Easy* in which they had sales of some $500,000. As this product competed both with the plaintiffs' *Miss Clairol Hair Color Bath* products and with the defendants' *Revlon* COLORSILK product it is not possible as I see it to conclude on the evidence that the plaintiffs suffered any loss of sales whatever by reason of the marketing of the defendants' product.

The plaintiffs' case is put in several ways. It was said first that the publication of the brochures and the use of the packages containing comparative color charts in which the plaintiffs' trade marks appeared constituted "use" of the plaintiffs' trade marks in such a way as to depreciate the value of the goodwill attaching thereto within the meaning of the prohibition of section 22(1) of the *Trade Marks Act*. Next it was said that the use of the plaintiffs' trade marks both in the defendants' brochures and on their packages constituted infringement of the exclusive right to the "use" throughout Canada of such trade marks which accrued to the plaintiffs under section 19 of the *Trade Marks Act* on the registration of the marks. Next it was said that the wording of the charts and packages constituted a description that was false, in several material respects which I shall mention later, and likely to mislead the public as to the character, quality, geographical origin and mode of performance of the wares and constituted unfair competition within the meaning of section 7(*d*) of the *Trade Marks Act*. Finally it was urged that the publication of the charts in the brochures and the use of them on the packages constituted an act or practice contrary to honest industrial or commercial usage in Canada and was unfair competition contrary to section 7(*e*) of the *Trade Marks Act*.

Apart from denial of the plaintiffs' assertions the defendants take the position that the use of color comparison charts was common both in the salon and retail hair coloring trades for many years prior to their introduction of the

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Revlon COLORSILK product in June 1965, that for a new product such as the *Revlon* COLORSILK product, particularly where it bore the name of a well known cosmetic line, the availability of a comparison chart for the purpose only of color selection in the new product is a useful and desirable aid and one that had been recognized in the industry in the past and that similar comparisons, in which the trade marks of competitors are also used for comparison purposes, were and are common in other branches of trade as well, including in particular the automotive and other replacement parts trades. As a further partial defence the defendants also raised an objection to which I shall refer later in these reasons to the validity of the registration of the trade mark *Hair Color Bath.*

I shall deal first with the points founded on section 7 of the Act. The section provides:

> 7. No person shall
>
> (*a*) make a false or misleading statement tending to discredit the business, wares or services of a competitor;
>
> (*b*) direct public attention to his wares, services or business in such a way as to cause or be likely to cause confusion in Canada, at the time he commenced so to direct attention to them, between his wares, services or business and the wares, services or business of another;
>
> (*c*) pass off other wares or services as and for those ordered or requested;
>
> (*d*) make use, in association with wares or services, of any description that is false in a material respect and likely to mislead the public as to
>
> (i) the character, quality, quantity or composition,
>
> (ii) the geographical origin, or
>
> (iii) the mode of the manufacture, production or performance of such wares or services; or
>
> (*e*) do any other act or adopt any other business practice contrary to honest industrial or commercial usage in Canada.

The first point founded on section 7(*d*) was that the wording complained of, particularly that on the defendants' packages, in fact represented to the purchasers that the product was approximately the same as the *Miss Clairol Hair Color Bath* product whereas in fact they were different in that the defendants' product was what is known as a *shampoo-in* product while that of the plaintiffs was not, that the fading qualities of the dyes differed and that different performance and results could be expected from them. In my view no such representation can properly be derived from the wording complained of and I do not think that anyone of ordinary intelligence would be likely to be misled by what is stated in any of the ways suggested. At most the statement might be taken to represent that the *Revlon* COLORSILK product would produce approximately the same shade as the *Clairol* product said to correspond with it but to my mind that is far from being a representation that the products or their quality or the mode of application were the same or even approximately the same.

Then it was said that the wording must also have been false since on Exhibits 4 and 8, the earliest package and the earlier brochure respectively, *Revlon* shade number 42, named Young Brown, was represented as corresponding approximately with *Clairol* shade number 46, named Chestnut Brown, whereas on Exhibits 5 and 9, the later package and brochure, the same *Clairol* shade was represented as corresponding approximately to *Revlon* shade number 48 named So True Ash Brown and not to *Revlon* shade number 42, Young Brown.

The basis of this submission was that *Revlon* shade 42 was described in both brochures (Exhibits 8 and 9) as a Warm Brown and *Revlon* shade 48 was described in the later of the two brochures (Exhibit 9) as a Medium Ash Brown. In this connection Mr. Robert Goldman, the president of the second named plaintiff, gave evidence that a color could not be warm brown and ash brown at the same time since warm brown has red or gold highlights whereas ash brown has very limited or no such highlights.

The explanation for the difference in the statements in the later brochure and packages given by Mr. Milton H. Schwarz, a chemist employed by a subsidiary of Revlon Inc. and vice president of its new products division, was that the *Revlon* shade number 42 was considered to correspond approximately with the *Clairol* shade number 46 when the first brochure and packages were put on the market but that Revlon Inc. later developed its shade number 48 which was considered to correspond more closely to the *Clairol* shade number 46 with which it was thereafter said to correspond approximately. The witness was not asked in cross-examination to comment on Mr. Goldman's statement that a color could not be a warm brown and an ash brown at the same time.

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There are undoubtedly some variations of shade between *Revlon* shades 42 and 48 and between each of them and *Clairol* shade 46 as the same are illustrated on Exhibits 3, 8 and 9 but the reproduction of colors in photographs in brochures was said to be not always exact and as the result to be expected from the use of hair coloring preparations depends on the color of the hair to which the product is to be applied and will therefore be subject to wide variation I am unable to attribute importance to such variations as I am able to observe, none of which would I regard as being of a major nature or beyond the range of tolerance that might be expected when an expression such as "approximately" is used. Moreover, while I am very conscious of my limitations in judging the significance of such matters as differences of shades of hair color I see no reason to think that the persons responsible for the statements would regard it as being in the interest of their employers to misrepresent to the public, whether deliberately or carelessly, the comparability of their shades with those of their competitors and having regard to the extensive measures taken to ensure and maintain the accuracy of the statements as well as to the fact that Mr. Schwarz, the person responsible for their accuracy, was not asked for an explanation as to how a warm brown and an ash brown could both be said to correspond approximately to the *Clairol* shade 46 I am not satisfied that either statement was in fact false.

Attacks under section 7(*d*) were also made on the grounds that the defendants' packages bore the name REVLON, INC., but nowhere gave the name of the first named defendant as their manufacturer as required by regulations made under the *Food and Drug Act* and, that on some of the packages the goods were represented as having been made in the United States when in fact they were made in Canada. In neither case am I of the opinion that the representation complained of is a material one.

I am accordingly of the opinion that the plaintiffs have not shown any cause of action based on section 7(*d*) of the *Trade Marks Act*.

A more serious attack was put forward based on section 7(*e*) of the Act but on consideration I am of the opinion that it too fails.

The case put forward was that in the circumstances the reference in the charts to the plaintiffs' products, which had been extensively advertised and had become well known to the public, was a device for describing the defendants' goods as equivalent to those of the plaintiffs and for obtaining the benefit of goodwill which the plaintiffs had built up over a long period of time by their efforts to produce a product of high quality and by massive expenditures on advertising. It was said that such goodwill was property of the plaintiffs and that to permit the defendants to take the benefit of it by describing their goods by reference to those of the plaintiffs would be to permit the defendants to unjustly enrich themselves at the plaintiffs' expense.

I do not find this submission unattractive in suggesting, as it does, as a standard to be applied for determining the honesty or otherwise of an act or practice in trading a concept already recognized by the law in other situations but I do not think it is the test which the statute calls for or prescribes. The particular statutory provision does not stand by itself but is the last of at least five separate prohibitions comprised in the section as a whole. It is, moreover, by its terms, applicable only to acts or practices of the nature prohibited other than those mentioned in the preceding paragraphs. The first of these preceding paragraphs is an express prohibition against making a false or misleading statement tending to discredit the business, wares or services of a competitor. In this the key words in my opinion are "false or misleading" and it is the falseness or deceptiveness of the statement which renders the statement dishonest and unfair. The corollory to this as I see it is that to make a statement that is neither false nor misleading is not prohibited even though it may tend to discredit the business, wares or services of a competitor. That this is the legal situation becomes plain I think when one considers that it never has been regarded, at least so far as I am aware, as dishonest or wrong for a business man to seek by any honest means to attract the customers of his competitors and thus to reduce the custom which they have theretofore enjoyed. The same thread appears to me to pervade paragraphs (*b*), (*c*) and (*d*), as well, of section 7, since each by its terms is limited to conduct which is deceptive or likely to result in deception and is in that

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sense dishonest. When therefore one comes to paragraph (*e*) and finds it prohibiting any other act or business practice contrary to honest industrial or commercial practice in Canada it seems clear that acts or practices that are dishonest in the sense of their being in some way deceptive or calculated to result in deception would fall within its purview. Acts or conduct involving some breach of trust or confidence[1] may well be considered to fall within that purview as well. But I do not think that in the context of the section as a whole the language used can properly be extended to prohibit conduct which can be regarded as dishonest only in the much more refined sense of taking advantage of a market situation even though that situation has been created, as in this case, largely by the efforts and expenditures of another so long as the means used to take advantage of the situation are not in themselves dishonest. The view of the scope of section 7(*e*) expressed by Schroeder J.A., speaking for the Court of Appeal of Ontario in *Eldon Industries Inc. v. Reliable Toy Co. Ltd.*[2] is, I think, to the same effect. There the learned judge said at page 123:

> Considerable argument was addressed to us as to the effect to be given to s. 7(*e*) of the *Trade Marks Act*. I am in agreement with the conclusion of the learned Judge of first instance that s. 7(*e*) must be read in conjunction with paras. (*a*), (*b*), (*c*) and (*d*) of that section: *A. C. Spark Plug Co. v. Canadian Spark Plug Service* [1935] Ex. C.R. 57, [1935] 3 D.L.R. 84; *Kitchen Overall & Shirt Co. v. Elmira Shirt & Overall Co.*, [1937] Ex. C.R. 230, [1938] 1 D.L.R. 7. These cases were decided under s. 11 of the *Unfair Competition Act*, 1932 (Can.), c. 38, which had codified the common law of passing off, and s. 7 of the *Trade Marks Act* is substantially a re-enactment of s. 11 of the *Unfair Competition Act* with some additions thereto. Section 7(*e*), therefore, must be read *ejusdem generis* with s. 7(*a*), (*b*), (*c*) or (*d*). The principles governing cases of product simulation have been carefully evolved both at common law and in equity and are now stated in statutory form in s. 7(*a*) to (*d*). They were never intended to yield to a subjective or unknown standard embraced in the words "any other business practice contrary to honest industrial or commercial usage in Canada", which would be the effect of the provisions of s. 7(*e*) if removed from the contextual influence of the foregoing clauses of the section. Furthermore, the *Copyright Act* and the *Industrial Design and Union Label Act* relating to designs confer a monopoly and limit both its duration and its scope in accordance with requirements expressly laid down by the statute, and it would not be right to place the broad construction on

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[1] *Vide Breeze Corporation v. Hamilton Clamp & Stamping Ltd.* (1961) 37 C.P.R. 153.

[2] (1965) 48 C.P.R. 109.

s. 7(*e*) urged by counsel for the appellants, since such an interpretation would be out of harmony with the scope and purpose of the relevant legislation which was designed to establish order and certainty in the regulation and control of monopolistic rights. In any event, the existence of a usage is a question of fact which must be proved in each case until eventually it becomes so well understood that the Courts take judicial notice of it, and there is no evidence in the present case which establishes any industrial or commercial usage which the defendants have contravened. Here the plaintiffs have failed to bring their design within the protection of the *Industrial Design and Union Label Act* and, as has been shown, the design is excluded from the ambit of the *Copyright Act.* Whatever may be said of the business ethics of a toy manufacturer or distributor in imitating designs of toys made by his competitors, if those designs do not enjoy statutory protection, then, unless he can be shown to have offended against the provisions of s. 7(*a*) to (*e*) of the *Trade Marks Act,* he has done no more than that which he had a legal right to do. An act lawful in itself is not converted by a malicious or bad motive into an unlawful act so as to make the doer of the act liable to a civil action: *Allen v. Flood,* [1898] A.C. 1. I share the view of the learned Judge of first instance that an act of dishonesty within the meaning of s. 7(*e*) of the *Trade Marks Act* which does not fall within the genus of acts prohibited by s. 7(*a*) to (*d*), which does not amount to breach of an express or implied contract, or which does not constitute a tortious act, is not actionable, and this ground of appeal should also fail.

As there was in my view nothing referring to the plaintiffs or their wares either in the defendants' brochures or on the defendants' packages which was calculated to deceive a purchaser and as the defendants were under no contractual or other obligation to refrain from seeking to attract the plaintiffs custom I am of the opinion that on the facts disclosed the plaintiffs have no cause of action based on any violation of section 7(*e*) of the Act.

I turn now to the allegations of infringement of the rights accruing to the plaintiffs under section 19 of the Act. The section provides that:

19. Subject to sections 21, 31 and 65, the registration of a trade mark in respect of any wares or services, unless shown to be invalid, gives to the owner the exclusive right to the use throughout Canada of such trade mark in respect of such wares or services.

As the plaintiffs' trade marks appear in the defendants' brochures and on their packages in the manner already described the question that arises on this section of the Act is one of the extent of the exclusive rights which accrue to the plaintiffs under it as a result of the registration of the marks. This turns on the interpretation to be put on the expression "the exclusive right to the use of such trade mark in respect of such wares" having regard to the definitions of

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"trade mark" and "use" in section 2 and to the provisions of section 4 which are incorporated by reference thereto as part of the definition of "use".

"Use" is defined in section 2(*v*) as meaning "any use that by section 4 is deemed to be a use in association with wares or services". With respect to wares section 4(1) provides:

> 4. (1) A trade mark is deemed to be used in association with wares if, at the time of the transfer of the property in or possession of such wares, in the normal course of trade, it is marked on the wares themselves or on the packages in which they are distributed or it is in any other manner so associated with the wares that notice of the association is then given to the person to whom the property or possession is transferred

Pausing here it is I think apparent that the presence of the plaintiffs' marks on the defendants' packages is a use of those marks "in association with" the wares in the defendants' packages within the meaning of section 4(1) because, and as I see it, simply because it is marked on the packages. The purpose for which it is there is, I think, irrelevant on this point which, as I read section 4 raises only the question of association or no association and states that association is to be deemed to exist in the three defined cases.[3] To my mind, however, the presence of the plaintiffs' marks on the comparative shade charts of the defendants' brochures is not a use of such marks within the

[3] A similar point was made by Lord Greene, M.R. in *Bismag Ld. v. Amblins (Chemists) Ld* (1940) 57 R P.C. 209 when he said at page 232:

> In Section 39 of the Act of 1905 the right conferred upon the proprietor of a registered trade mark is stated to the "the exclusive right to the use of such trade mark upon or in connection with the goods in respect of which it is registered". If therefore A was the registered proprietor of a trade mark for "Chemical substances prepared for use in medicine and pharmacy" (Class 3), B could not use that trade mark upon or in connection with substances of this character manufactured by B. By this was meant, as appears from the Yeast-Vite case, that before a use by B of the trade mark in relation to his own goods could amount to an infringement, it must be shown that such use was for the purpose of indicating the origin, of these very goods in the user of the mark, that is, B. In the Yeast-Vite case the defendant's use was, I should have thought, clearly a use "in relation to" the defendant's own goods, according to the ordinary meaning of that phrase apart from any special context—a meaning which appears to have commended itself to Lord *Tomlin* in the passage from his speech quoted above. The plaintiff failed because the defendant's use of the mark, although it was a use in relation to the defendant's own goods, was not for the purpose of indicating the origin of those goods in the user of the mark, that is, the defendant.

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meaning of section 4(1) since the brochures are neither the wares themselves nor the packages in which the wares are distributed and nothing that I would regard as notice to any person purchasing the defendants' wares of any association of the plaintiffs' marks with those wares, so far as I am aware, ever occurs in any use to which the brochure or its chart can be put at the time of the transfer of the property or possession of the defendants' goods to their purchaser.

"Trade mark" is defined in section 2(*t*) as follows:

> 2. In this Act
>
> (*t*) "trade mark" means
>
> (i) a mark that is used by a person for the purpose of distinguishing or so as to distinguish wares or services manufactured, sold, leased, hired or performed by him from those manufactured, sold, leased, hired or performed by others,
>
> (ii) a certification mark,
>
> (iii) a distinguishing guise, or
>
> (iv) a proposed trade mark,

The expressions in (ii), (iii) and (iv) of this definition[4] are also defined, in the cases of (iii) and (iv) in terms precisely similar to those in (1), and in the case of (ii) in

[4] 2. In this Act,

(*a*) "certification mark" means mark that is used for the purpose of distinguishing or so as to distinguish wares or services that are of a defined standard with respect to

(i) the character or quality of the wares or services,

(ii) the working conditions under which the wares have been produced or the services performed,

(iii) the class of persons by whom the wares have been produced or the services performed, or

(iv) the area within which the wares have been produced or the services performed,

from wares or services that are not of such a defined standard;

(*g*) "distinguishing guise" means

(i) a shaping of wares or their containers, or

(ii) a mode of wrapping or packaging wares

the appearance of which is used by a person for the purpose of distinguishing or so as to distinguish wares or services manufactured, sold, leased, hired or performed by him from those manufactured, sold, leased, hired or performed by others;

(*m*) "proposed trade mark" means a mark that is proposed to be used by a person for the purpose of distinguishing or so as to distinguish wares or services manufactured, sold, leased, hired or performed by him from those manufactured, sold, leased, hired or performed by others;

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terms that are similar but define the purpose as being to distinguish by a standard rather than by origin. In all cases, however, a trade mark is defined by reference to use for the purpose of distinguishing or so as to distinguish wares or services whether of a particular origin or of a defined standard, from others. When therefore section 19 provides that the registration of a trade mark in respect of any wares or services gives to the owner "the exclusive right to the use of such trade mark throughout Canada in respect of such wares or services" what it appears to me to confer is the exclusive right to the use of such mark in association with such wares or services (within the meaning of sections 2(*v*) and 4) for the purpose of distinguishing the wares or services as being those of the user of the trade mark or of a defined standard from others. A use of the mark, in association with wares or services, within the meaning of sections 2(*v*) and 4, that is not "for the purpose of distinguishing or so as to distinguish" the particular wares or services from others is not, however, as I see it within the area of the exclusive right conferred by section 19.

In this respect the law is I think the same as the English law under the *Trade Marks Act,* 1905. That Act defined trade mark as a mark "used or proposed to be used upon or in connection with goods for the purpose of indicating that they are the goods of the proprietor of such trade mark", etc. and it gave to the proprietor of such a mark when registered "the exclusive right to the use of such trade mark upon or in connection with" the goods in respect of which it was registered. In *Irving's Yeast-Vite Ltd. v. F. A. Horsenail*[5], a case having some parallels on the facts with the present, in particular in that the plaintiffs' mark appeared on the defendants' goods for the purpose of comparing the goods with goods of the plaintiff, the Courts held that such a use was not within the exclusive right conferred by the statute. In the House of Lords Lord Tomlin said at page 115:

> Now the act which the Appellants contend amounts in law to an infringement of their exclusive right as registered proprietors of the Trade Mark is the use by the Respondent upon the bottles in which he sells his preparation of the phrase "Yeast Tablets, a substitute for Yeast-Vite."

[5] (1934) 51 R.P.C. 110.

This is clearly a use of the word "Yeast-Vite" on the Respondent's preparation to indicate the Appellant's preparation and to distinguish the Respondent's preparation from it. It is not a use of the word as a trade mark, that is, to indicate the origin of the goods in the Respondent by virtue of manufacture, selection, certification, dealing with or offering for sale.

It is therefore essential for the Appellants to establish that the construction put upon Section 39 by the Court of Appeal in this case and in the earlier cases is wrong.

The Appellants say that Section 39 of the Act of 1905 confers an exlusive right to the use of the trade mark upon or in connexion with the goods in respect of which it is registered, and that therefore, where the trade mark is a word, that word cannot be used by anyone else upon or in connexion with such goods even though the use is in a phrase or sentence intended to indicate that the goods are not goods originating with the owner of the registered mark.

The contention may be put in another way, namely, that to constitute an infringement of the exclusive right conferred by Section 39 it is not necessary that the word should be used by the alleged infringer as a trade mark, that is for the purpose of indicating that the goods have "by virtue of manufacture, selection, certification, dealing with or offering for sale" their origin with him who employs the word

The Appellants support their view by calling attention to (1) the fact that Section 39 does not contain any words defining or limiting the purpose of the user corresponding to the words indicating purpose appearing in the definition of "Trade Mark" contained in Section 3 of the same Act, (2) the fact that certain defences to a claim of infringement are made expressly available by the Act, and (3) the contrast between the language employed in Section 39 and that employed in Section 4 of the Act of 1919 with reference to trade marks in Part B of the register.

They accordingly urge that the exclusive right conferred by Section 39 is not confined to user in relation to any particular purpose and that the claim to enforce the right cannot be met by any defence outside those arising expressly under the provisions of the statutes.

* * *

It is true that the language of the definition of a trade mark contained in Section 3 of the Act of 1905 cannot without some change of form be read directly into Section 39, but it is equally true that the language of Section 39 must carry with it some implied limitation, unless it is to be given a meaning extending its operation although outside the scope of the *Trade Marks Acts*.

The phrase "the exclusive right to the use of such trade mark" carries in my opinion the implication of use of the mark for the purpose of indicating in relation to the goods upon or in connection with which the use takes place, the origin of such goods in the user of the mark by virtue of the matters indicated in the definition of "trade mark" contained in Section 3.

Here, in my view, this element is not present. As already mentioned the marks, *Revlon* and COLORSILK, appear prominently on the top, bottom and all four sides of the

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defendants' packages as well as in the chart and the marks *Miss Clairol* and *Hair Color Bath,* which appear only in the chart, appear in smaller print than the marks, *Revlon,* and COLORSILK. The chart moreover is headed COMPARATIVE HAIR COLOR SHADE CHART, followed by the words *The sparkling, natural-looking Revlon Hair Color Shades correspond approximately to the competitive shades indicated.* In these circumstances, it is, I think, abundantly clear from looking at the packages that the marks, *Miss Clairol* and *Hair Color Bath,* are not intended to indicate and do not indicate to anyone that the contents of the package are the defendants' goods. Nor do I think it likely that any prospective purchaser of a package of these wares would be likely to be deceived by the presence of the marks, *Miss Clairol* and *Hair Color Bath,* as they appear on the package, into thinking that they were intended to indicate the origin of the goods in the package.

If, as I think, this is the correct interpretation of section 19 the conclusion that the plaintiffs' exclusive rights under the section are not infringed applies *a fortiori* so far as the brochures complained of and the presence of the plaintiffs' trade marks in the comparative shade charts contained therein are concerned since in the case of these charts neither of the elements I have mentioned is present.

On this ground of attack as well, therefore, the plaintiffs' case, in my opinion, fails. It is, however, in my view, of some importance to bear in mind that in the case of the packages the attack failed not because the trade marks were not used "in association with" the defendants' goods within the meaning of sections 2(v) and 4(1) but because the use made of them "in association with" the defendants' goods was not a use for the purpose of distinguishing the goods as goods of the defendants and for that reason alone was not a use the exclusive right to which had been conferred on the plaintiffs by section 19.

This brings me to the remaining ground put forward, that is to say, that the defendants in having the plaintiffs' marks on their packages and in their brochures are using the plaintiffs' trade marks "in a manner likely to have the effect of depreciating the value of the goodwill attaching thereto" within the meaning of the prohibition of section 22(1) of the Act.

Section 22 is a new section in the 1952-53 statute and thus far, so far as I am aware, there have been no decided cases in which it has been applied. Nor am I aware of any similar provisions having been enacted in any other country. There would be I think no difficulty in concluding that the section would find application in cases of the use of a well known trade mark by someone other than its registered owner but in a non-competing field of trade or in association with wares or services in respect of which it is not registered. It may be observed of this type of case that the use of the trade mark might, though it would not necessarily, be deceptive. Deception, however, is not the test prescribed by section 22, rather the test is the likelihood of depreciating the value of the goodwill attaching to the trade mark, a result which would not necessarily flow from deception and which might result without deception being present. In any event the present is not a situation of the type mentioned and the question remains whether the section applies to it.

In its ordinary sense the language of section 22(1) is, I think, broad enough to embrace uses likely to have the result of depreciating goodwill which are far removed from the type of case I have mentioned. Indeed in its ordinary sense the language seems broad enough to include a conversation in which a person adversely criticizes goods which he identifies by reference to their trade mark. I regard it as highly unlikely, however, that so broad a prohibition could have been intended. In the course of his argument Mr. Henderson treated the meaning of "use" as referring to use only in competitive trading, but while I think that use in the course of trading is a limitation which is obviously present, the statute being one relating to trade marks and unfair competition, this too would leave very wide scope for the prohibition. There are many common instances of the use of trade marks in the course of trading which I do not think the section could have been intended to prohibit. A trade mark is "used", for example, in this sense in the course of trade when a shopkeeper exhibits a poster on his counter or in his shop with a comparative price list indicating by reference to their trade marks the goods of several traders who may be competitors of one another. It is also used in this sense in the course of trade when a sales clerk makes reference to it in the course of

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discussing the merits of the owner's goods with a customer, whether in comparison with the goods of other traders or not. Such uses could, depending on what was being said, tend to adversely affect the goodwill attaching to a trade mark but I do not think the statute is intended to forbid legitimate comparisons or criticisms of that kind. Rather I think the verb "use" in section 22 is to be interpreted by reference to the definition of the noun "use" in section 2(*v*) the effect of which is to confine the application, and therefore the prohibition, of section 22 to a use which any person may make, in association with goods or services within the meaning of the subsections of section 4, of another's registered trade mark, in such a manner as to depreciate the value of the goodwill attaching thereto.

As applied to a case of this kind section 22(1) might in accordance with this interpretation be read as follows:

> No person shall use in association with wares within the meaning of section 4 a mark that is used by another person for the purpose of distinguishing or so as to distinguish wares manufactured etc. by him from those manufactured etc. by others and which mark has been registered by him as his trade mark, in a manner likely to depreciate the value of the goodwill attaching thereto.

If, as I think, this is the correct way to interpret the verb "use" in section 22(1) it follows from what I have already said when considering section 4 that the presence of the plaintiffs' trade marks on the defendants' packages is within the meaning of "use" in section 22(1) but that their presence in the defendants' brochures is not within it. It remains, however, to consider whether the use so made of the plaintiffs' marks on the defendants' packages is use in a manner likely to depreciate the value of the goodwill attaching to the plaintiffs' marks.

This raises as well for the first time, so far as I am aware, the question of what is to be regarded as the goodwill attaching to a trade mark. The goodwill of a business is a well known concept but the goodwill attaching to a trade mark is I think not likely to be quite the same or to be as extensive as the goodwill of the business in which it is used save possibly in the rare case where all the goods sold in the course of the business bear a particular trade mark and the location where the business is carried on has no significance at all in attracting former or new customers.

In *Trego v. Hunt*[6] Lord Herschell in discussing the meaning of goodwill of a business, after referring to a statement by Lord Eldon in *Cruttwell v. Lye* that "the goodwill which has been the subject of sale is nothing more than the probability that the old customers will resort to the old place" proceeded thus at page 17:

> If the language of Lord Eldon is to be taken as a definition of goodwill of general application, I think it is far too narrow, and I am not satisfied that it was intended by Lord Eldon as an exhaustive definition.
>
> "'Goodwill', I apprehend", said Wood V.-C. in *Churton v. Douglas* "must mean every advantage—every positive advantage, if I may so express it, as contrasted with the negative advantage of the late partner not carrying on the business himself—that has been acquired by the old firm in carrying on its business, whether connected with the premises in which the business was previously carried on, or with the name of the late firm, or with any other matter carrying with it the benefit of the business". The learned Vice-Chancellor pointed out in this connection that it would be absurd to say that when a large wholesale business is conducted the public are mindful whether it is carried on in Fleet Street or in the Strand.
>
> The question, what is meant by "goodwill", is, no doubt, a critical one. Sir George Jessel, discussing in *Ginesi v. Cooper* the language of Wood V.-C. which I have just quoted, said: "Attracting customers to the business is a matter connected with the carrying of it on. It is the formation of that connection which has made the value of the thing that the late firm sold, and they really had nothing else to sell in the shape of goodwill." He pointed out that, in the case before him, the connection had been formed by years of work. The members of the firm knew where to sell the stone, and he asks: "Is it to be supposed that they did not sell that personal connection when they sold the trade or business and the goodwill thereof?"
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> The present Master of the Rolls took much the same view as to what constitutes the goodwill of a business. I cannot myself doubt that they were right. It is the connection thus formed, together with the circumstances, whether of habit or otherwise, which tend to make it permanent, that constitutes the goodwill of a business. It is this which constitutes the difference between a business just started, which has no goodwill attached to it, and one which has acquired a goodwill. The former trader has to seek out his customers from among the community as best he can. The latter has a custom ready made. He knows what members of the community are purchasers of the articles in which he deals, and are not attached by custom to any other establishment.

Lord Macnaghten also said at page 23:

> What "goodwill" means must depend on the character and nature of the business to which it is attached. Generally speaking, it means much more than what Lord Eldon took it to mean in the particular

6 [1896] A.C. 7.

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case actually before him in *Cruttwell v. Lye,* where he says: "the goodwill which has been the subject of sale is nothing more than the probability that the old customers will resort to the old place" Often it happens that the goodwill is the very sap and life of the business, without which the business would yield little or no fruit. It is the whole advantage, whatever it may be, of the reputation and connection of the firm, which may have been built up by years of honest work or gained by lavish expenditure of money.

Lord Macnaghten considered the question again a few years later in *Inland Revenue Commissioners v. Muller & Co.'s Margarine, Limited*[7] where at page 223 he said:

> What is goodwill? It is a thing very easy to describe, very difficult to define. It is the benefit and advantage of the good name, reputation, and connection of a business. It is the attractive force which brings in custom. It is the one thing which distinguishes an old-established business from a new business at its first start. The goodwill of a business must emanate from a particular centre or source. However widely extended or diffused its influence may be, goodwill is worth nothing unless it has power of attraction sufficient to bring customers home to the source from which it emanates. Goodwill is composed of a variety of elements. It differs in its composition in different trades and in different businesses in the same trade. One element may preponderate here and another element there.
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> * * *
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> For my part, I think that if there is one attribute common to all cases of goodwill it is the attribute of locality. For goodwill has no independent existence. It cannot subsist by itself. It must be attached to a business. Destroy the business, and the goodwill perishes with it, though elements remain which may perhaps be gathered up and be revived again. No doubt, where the reputation of a business is very widely spread or where it is the article produced rather than the producer of the article that has won popular favour, it may be difficult to localise goodwill.

I have quoted from these cases at some length because in my opinion the goodwill attaching to a trade mark referred to in section 22, while not necessarily the same as or co-extensive with the meaning of goodwill as applied to a business, is made up of similar elements. The element of the location from which the goods bearing the trade mark emanate is, at least in the case of widely advertised marks such as the plaintiffs, in my view, of comparatively little importance. The place or places could I think in such cases be changed within rather wide limits with comparatively little effect on the goodwill attaching to the trade mark. But the element of the likelihood of a satisfied purchaser of goods bearing the trade mark purchasing goods again by

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[7] [1901] A.C. 217.

reference to it is I think a large element of the goodwill attaching to it. The likelihood that such customers will tell their friends of their satisfaction with the product is I think another element of it. Yet another element is the effect of such persuasion to purchase the product as advertising may achieve whether to attract new customers or to induce former customers to continue to use the product identified by the mark. To paraphrase Lord Macnaghten's expression in *Trego v. Hunt*[8] the goodwill attaching to a trade mark is I think that portion of the goodwill of the business of its owner which consists of the whole advantage, whatever it may be, of the reputation and connection, which may have been built up by years of honest work or gained by lavish expenditure of money and which is identified with the goods distributed by the owner in association with the trade mark.

Then what is meant by "depreciate the value" of such goodwill. To my mind this means simply to reduce in some way the advantage of the reputation and connection to which I have just referred, to take away the whole or some portion of the custom otherwise to be expected and to make it less extensive and thus less advantageous. As I see it goodwill has value only to the extent of the advantage of the reputation and connection which its owner enjoys and whatever reduces that advantage reduces the value of it. Depreciation of that value in my opinion occurs whether it arises through reduction of the esteem in which the mark itself is held or through the direct persuasion and enticing of customers who could otherwise be expected to buy or continue to buy goods bearing the trade mark. It does not, however, as I see it, arise, as submitted by Mr. Henderson, from danger of loss of exclusive rights as a result of use by others as this in my view represents possible loss of exclusive rights in the trade mark itself rather than reduction of the goodwill attaching to it.

I have already expressed the opinion that it has not heretofore been considered to be dishonest for a person in business to seek by honest means to attract away the customers of a competitor and thus to reduce the custom which the competitor enjoys. The right to do this, however, if it can be called a right, is, as indicated, dependant on

[8] [1896] A.C. 7.

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the honesty of the means used and cases such as *Trego v. Hunt*[9] point out the limits to which at common law and in equity such means might go. Thus in that case, which was concerned with the rights of one of the vendors of an established business in starting up a new business in competition with that sold, Lord Herschell said at page 20:

> It is often impossible to draw the line and yet possible to be perfectly certain that particular acts are on one side of it or the other. It does not seem to me to follow that because a man may, by his acts, invite all men to deal with him, and so, amongst the rest of mankind, invite the former customers of the firm, he may use the knowledge which he has acquired of what persons were customers of the old firm in order, by an appeal to them, to seek to weaken their habit of dealing where they have dealt before, or whatever else binds them to the old business, and so to secure their custom for himself. This seems to me to be a direct and intentional dealing with the goodwill and an endeavour to destroy it. If a person who has previously been a partner in a firm sets up in business on his own account and appeals generally for custom, he only does that which any member of the public may do, and which those carrying on the same trade are already doing. It is true that those who were former customers of the firm to which he belonged may of their own accord transfer their custom to him; but this incidental advantage is unavoidable, and does not result from any act of his. He only conducts his business in precisely the same way as he would if he had never been a member of the firm to which he previously belonged. But when he specifically and directly appeals to those who were customers of the previous firm he seeks to take advantage of the connection previously formed by his old firm, and of the knowledge of that connection which he has previously acquired, to take that which constitutes the goodwill away from the persons to whom it has been sold and to restore it to himself.

This passage appears to me to parallel very closely a concept which I think is implicit in and to have been intended by section 22(1). The person referred to in section 22(1) is not one who is under any disability by reason of his having sold or been party to the sale of the goodwill referred to but he is prohibited by the statute from using, in the sense that I have indicated, the trade mark of another in a manner likely to have the effect of depreciating the goodwill attaching thereto. He may of course put information on his wares for the purpose of telling customers about his own wares in order to get the customers to buy them in preference to those of the owner of a particular trade mark. In general how he may do that is left to his own ingenuity and provided the means adopted are honest

9 [1896] A.C. 7.

means no one can challenge him. But he may not put his competitor's trade mark on his goods for that purpose or for the purpose of carrying a message to customers who are familiar with the goods identified by the trade mark in order to facilitate their purchase of his own goods and thus to reduce the chance that new customers hearing of the goods identified by the mark would buy them in preference to his or that old customers familiar with the goods identified by the trade mark would have continued buying the goods of the owner of the mark. In short he may not use his competitor's trade mark for the purpose of appealing to his competitor's customers in his effort to weaken their habit of buying what they have bought before or the likelihood that they would buy his competitor's goods or whatever binds them to his competitor's goods so as to secure the custom for himself, for this is not only calculated to depreciate and destroy his competitor's goodwill but is using his competitor's trade mark to accomplish his purpose.

Here as I see it all the elements necessary for the application of section 22 are present. The plaintiffs have what is admittedly a well known registered trade mark, *Miss Clairol,* to which I have no doubt a substantial body of goodwill is attached. They have as well the registered trade mark, *Hair Color Bath,* which it appears was registered in October 1961 after satisfying the Registrar of its distinctiveness. It had been used before that and has been extensively used since then. On the facts therefore I see no reason to doubt that some body of goodwill, the extent of which it appears to me to be unnecessary to attempt to assess, is attached to it as well. The defendants have both of these trade marks on the packages in which their wares are distributed and are thus using the marks in association with their wares within the meaning of section 4. They do this for the purpose of facilitating persons familiar with the plaintiffs' products to switch to using their products. Whether the purpose is legitimate or not it is not the name of the plaintiff but the plaintiffs' trade marks that are used for this purpose. That this is a course of conduct which would be likely to depreciate the goodwill attaching to the plaintiffs' marks is I think obvious but even that is made overwhelmingly clear by the fact that of all the

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persons competing in the hair color trade it is only the plaintiffs whose marks are used in the comparison charts on the defendants' packages, by the evidence of Mr. Thomas that the purpose of putting the charts on the packages was to promote the sale of their goods and by the evidence of Mr. Schwarz, who was the party responsible for the preparation of the wording on the packages, that the purpose was to suggest to customers that they could get approximately the same result from using a *Revlon* COLORSILK product as from the corresponding *Clairol* product in the hope of getting a part of the market enjoyed by the plaintiffs who represented the dominant competition in the field. When parties have done what is complained of for the express purpose of taking away custom enjoyed by competitors and persist in it I see no reason to doubt that they are succeeding in their purpose.

I am accordingly of the opinion that the use made by the defendants of the plaintiffs' trade marks *Miss Clairol* and *Hair Color Bath* on its packages was and is a use of them in a manner likely to depreciate the value of the goodwill attaching thereto within the meaning of section 22(1) of the Act and that the plaintiffs are entitled to relief in respect thereof.

In the course of the trial evidence was given of the use by traders for various purposes of trade marks of others in catalogues and on their wares or the packages in which they are distributed in several other fields of trade, particularly in the automotive and other replacement parts fields, and it was submitted that the prevalence of this practice indicated that it was not objectionable or within the purview of what is prohibited by section 22(1). I do not regard it as necessary, however, for the purposes of this case, to consider the alleged practice. Obviously no such practice can lawfully prevail if it is contrary to the statute but in any event there are differences in the facts pertaining to each particular example offered in evidence when compared with the facts of the present situation and with each other. Whether these differences would make a difference in result if the owners of the particular trade marks sought to prevent the practice could, as I see it, be determined only if the question were properly raised and I do not think it aids the determination of this case to make an assumption of the legality of the alleged practice and found any conclusion thereon. It should be clear that I express no opinion with respect to any of the examples in question.

The defendants raised by way of a partial defence the submission that the registration of the trade mark *Hair Color Bath* was invalid because the trade mark had never been used separately from the trade mark *Miss Clairol* and therefore could not have been distinctive at the time when it was registered. It was, however, established that the trade marks have appeared separately in a number of magazine advertisements, at least one of which was published before and the remainder since the registration of the trade mark, and that both in magazine advertisements and in the printed matter on the plaintiffs' packages distinctions are made by having the two marks in different sizes of type, usually in different colors of type and invariably with asterisks and footnotes indicating that they are separate trade marks. This in my view contradicts the defendants' assertion. The defence, accordingly, in my opinion has not been established.

It was also submitted that the present is a case in which the discretion of the Court under section 22(2) to decline to award damages or order an accounting of profits should be exercised in the defendants' favour. It is established, however, that the defendants' use of the plaintiffs' marks on its packages was part of a calculated plan to profit from the reputation and goodwill of the plaintiffs, who, at that time as a result of their earlier efforts to promote the sale of their products, enjoyed the bulk of the market. To excuse a defendant from payment for the consequences of his conduct in such circumstances would seem to me to be an open invitation to traders to act accordingly until stopped and I cannot think that to be the kind of case in which it was intended that the defendant should be excused.

In the result therefore the plaintiffs are entitled to relief in respect of the distribution by the defendants in the course of trade of hair color preparations in packages bearing color comparison charts which include the trade marks *Miss Clairol* and *Hair Color Bath* and I will hear the parties on the forms of the relief as well as on the subject of costs when application is made for judgment.

Montreal 1968 June 25 — Ottawa July 2

BETWEEN:

HER MAJESTY THE QUEEN ....PLAINTIFF;

AND

ALEXIS NIHON ....DEFENDANT.

Expropriation—Deposit of plan—Statutory presumption that described land necessary for public work—Not reviewable by court—Expropriation Act, s. 12—Canadian National Montreal Terminals Act, S. of C. 1929, c. 12.

Section 12 of the *Expropriation Act* provides that the filing of a plan of land taken for a public work shall be deemed to indicate that in the expropriating Minister's judgment such land is necessary for that work.

Defendant landowner alleged in its statement of defence that not all of the land taken was necessary for the public work contemplated.

Held, the allegation should be struck out. The Minister's judgment that the land was necessary is not reviewable.

The King v. Toronto [1946] Ex. C R. 424, followed; *Boland v. C.N.R.* [1927] A.C. 198, distinguished. *Canadian National Railways Act,* S of C 1919, c. 13, s. 13; R.S.C. 1927, c 172, s. 17, am. 1929, c. 10, s. 2; *Canadian National Montreal Terminals Act* S. of C. 1929, c. 12, ss. 7, 9 considered.

APPLICATION.

André Perrault for plaintiff.

R. H. Walker, Q.C. and *John H. Gomery* for defendant.

JACKETT P.:—An application was made before me herein at Montreal on Tuesday, June 25, 1968, to strike out certain portions of the statement of defence (including certain paragraphs in the "particulars" of the defence).

The action was instituted by the Attorney General of Canada under the *Expropriation Act* to have the compensation for land taken under that Act determined and the portions of the defence that are the subject matter of the motion to strike out are the portions thereof whereby the defendant attacks the expropriation as having been invalid in whole or in part because the lands "alleged to have been taken" were not "to their full extent, necessary for the public work contemplated in the statement of claim". Apart from one respect to which I will refer hereafter, counsel for the defendant made it clear that the provisions in the defence that are attacked were not intended to raise any attack on the validity of the expropriation except attacks based on the contention that some part or all of the lands that were the subject of the expropriation procedures were unnecessary for the public work for which they were said to have been taken. In other words, no question is raised as to the various steps contemplated by the *Expropriation Act* to take land having been duly taken. In these circumstances, the plaintiff's motion is based on section 12 of the *Expropriation Act*, which reads as follows:

> 12. In all cases, when any such plan and description, purporting to be signed by the deputy of the minister, or by the secretary of the department, or by the superintendent of the public work, or by an engineer of the department, or by a land surveyor duly licensed as aforesaid, is deposited of record as aforesaid, the same shall be deemed and taken to have been deposited by the direction and authority of the minister, and as indicating that in his judgment the land therein described is necessary for the purposes of the public work; and the said plan and description shall not be called in question except by the minister, or by some person acting for him or for the Crown.

The plaintiff says in effect, as I understand it, that, when a plan and description purporting to be signed by the deputy of the appropriate minister has been duly deposited of record under the *Expropriation Act*, section 12 operates, *inter alia*, as

(a) a statutory requirement that it shall be taken as indicating that "in his judgment" (i.e., the judgment of the minister) "the land therein described is necessary for the purpose of the public work", and

(b) a statutory prohibition against the plan and description being called in question by any person other than "the minister, or by some person acting for him or for the Crown".

Superficially, section 12 appears to be applicable here. The defendant admits that a plan and description signed by the deputy of the appropriate minister was duly deposited in the manner contemplated by the *Expropriation Act*, but nevertheless attacks the validity of the expropriation in whole or in part on the basis of an allegation that the lands described in the plan and description "were not, to their full extent, necessary" for the "work". Section 12, as it has been interpreted by this Court, would appear to prohibit any person other than the minister or some person

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acting for the Crown making any such attack. See *The King v. City of Toronto et al*[1] and *The King v. North York Township et al.*[2]

However, the matter cannot be disposed of so summarily because the decision of the Privy Council in *Boland v. Canadian National Railway Company*[3] indicates that there can be circumstances in which the Court must consider whether land described in a plan and description filed in the manner provided by the *Expropriation Act* was validly taken for a work for which it could be expropriated under that Act.

Before proceeding to consider the matter in detail, I should say that, after hearing counsel on the question whether the question should be dealt with at this stage or left for consideration by the trial judge, I came to the conclusion, and I think counsel for both parties were in agreement, that it was a question that should be decided before the parties should proceed to discovery or trial. This is a very substantial expropriation case. The Crown is willing to pay $60,636.20 and the defendant claims over $2,000,000. The expropriation took place over seventeen years ago. The claim of the defence involves the Court in an investigation of "a large real estate development plan" upon which the defendant says that it had embarked before the expropriation. The case is related to another case (No. 141672) between the same parties in which the amounts involved are even larger and in which the same general problems arise. In my view, it will be difficult enough, for the Court and for counsel, to conduct a trial or trials of these two cases on the compensation questions without it being necessary to try at the same time the very intricate and difficult question of fact as to what lands are or were "necessary" for the Canadian National Montreal Terminal. In my view, the question of law as to whether section 12 operates to prohibit the Court from embarking on any such inquiry should be determined in advance of discovery and trial so that the trial or trials of the compensation questions will not become involved with a substantial inquiry concerning facts that are otherwise irrelevant unless the Court is properly concerned with them.

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[1] [1946] Ex. C.R. 424. [2] [1948] 2 D.L.R. 381.
[3] [1927] A.C. 198.

Before examining the pleadings in this action, it may be helpful to refer to legislation some knowledge of which is necessary to understand the background.

The *Expropriation Act*[4] has remained unchanged, with one irrelevant exception, since the Revised Statutes of 1906 (chapter 143). The courts have uniformly proceeded on the view that this statute authorizes the Crown to expropriate land by the filing of a plan and description of the land to be taken in the appropriate registry office, although the statute is not as appropriately worded to achieve that end as it might be. Section 3(*b*) authorizes the Minister (who, by definition, is the head of a department charged with the construction and maintenance of a public work) to "enter upon and take possession of any land...the appropriation of which is, in his judgment, necessary for...the public work". Section 9(1) then contains two apparently separate provisions, although they are linked together by cross references in one to the other. They are

(a) "Land taken for the use of Her Majesty shall be laid off by metes and bounds"; and

(b) "when no proper deed or conveyance thereof to Her Majesty is made...or when, for any other reason, the Minister deems it advisable so to do, a plan and description of such land signed by the Minister ...shall be deposited of record in the office of the registrar of deeds for the county...in which the land is situate, *and such land, by such deposit, shall thereupon become and remain vested in Her Majesty.*

(The italics are mine.)

It is in relation to these provisions in section 9 that section 12, which I have already quoted, must be read. For convenience, I repeat that section here.

> 12. In all cases, when any such plan and description, purporting to be signed by the deputy of the minister, or by the secretary of the department, or by the superintendent of the public work, or by an engineer of the department, or by a land surveyor duly licensed as aforesaid, is deposited of record as aforesaid, the same shall be deemed and taken to have been deposited by the direction and authority of the minister, and as indicating that in his judgment the

4 R S C. 1952, chapter 106.

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land therein described is necessary for the purposes of the public work; and the said plan and description shall not be called in question except by the minister, or by some person acting for him or for the Crown.

While the opening words of section 9 seem to contemplate that land will already have been "taken for the use of Her Majesty" before the necessity of filing a plan and description arises, section 12 seems to provide that it is unnecessary to inquire whether any such prior taking has occurred once a "plan and description", duly signed, has been deposited.

The next statute to which reference should be made is the *Canadian National Railways Act.*[5] That statute recited that it was expedient to provide for the incorporation of a company under which the railways of the Canadian Northern system might be consolidated, and together with the Canadian Government railways operated as a national railway system. After providing for the constitution of the Canadian National Railway Company, the statute provided (section 11) for entrusting to that company by order in council the management and operation of any railways or other properties owned, controlled or occupied by Her Majesty, for the transfer to that company of the stocks in railway companies which the Crown had previously acquired, or might thereafter acquire (section 12), and for the construction and operation by that company of new railways (section 23). Section 13 of the 1919 Act[6] provided *inter alia* for using the *Expropriation Act* for acquiring land for the Company's undertaking. Section 13 read as follows:

> 13. (1) All the provisions of the *Railway Act* (excepting those provisions which are inconsistent with this Act, and excepting also the provisions of the *Railway Act* relating to the location of lines of railway, the making and filing of plans and profiles—other than highway and railway crossing plans—and the taking or using of lands) shall apply to the Company and its undertaking, it being declared that all the provisions of the *Expropriation Act,* except where inconsistent with this Act, apply *mutatis mutandis* to the Company and its undertaking, in lieu of the provisions of the *Railway Act* so excepted.
>
> (2) With respect to the undertaking of the Company,—
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> (*a*) Any plan deposited under the provisions of the *Expropriation Act* may be signed by the Minister of Railways and

5 S. of C. 1919, c. 13; R.S.C. 1927, c. 172.

6 Sec. 17 of R.S.C. 1927, c. 172.

Canals on behalf of the Company, or by the President or any Vice-President of the Company; no description need be deposited;

(b) The land shown upon such plan so deposited shall thereupon be and become vested in the Company, unless the plan indicates that the land taken is required for a limited time only or that a limited estate or interest therein is taken; and by the deposit in such latter case the right of possession for such limited time or such limited estate or interest shall be and become vested in the Company;

(c) The compensation payable in respect of the taking of any lands so vested in the Company, or of interests therein, or injuriously affected by the construction of the undertaking or works shall be ascertained in accordance with the provisions of the *Railway Act*, beginning with notice of expropriation to the opposite party.

Section 13[7] was repealed by chapter 10 of the Statutes of 1929 and the following was substituted therefor:

17. (1) All the provisions of the *Railway Act* shall apply to the Company, except as follows:—

(a) such provisions as are inconsistent with the provisions of this Act;

(b) the provisions relating to the location of lines of railway and the making and filing of plans and profiles, other than highway and railway crossing plans;

(c) such provisions as are inconsistent with the provisions of the *Expropriation Act* as made applicable to the Company by this Act.

(2) (a) All the provisions of the *Expropriation Act*, except where inconsistent with the provisions of this Act, shall apply *mutatis mutandis* to the Company;

(b) Any plan deposited under the provisions of the *Expropriation Act* may be signed by the Minister of Railways and Canals on behalf of the Company, or by the President or any Vice-President of the Company; no description need be deposited;

(c) The land shown upon such plan so deposited shall thereupon be and become vested in the Company, unless the plan indicates that the land taken is required for a limited time only or that a limited estate or interest therein is taken; and by the deposit in such latter case the right of possession for such limited time or such limited estate or interest shall be and become vested in the Company;

(d) The compensation payable in respect of any lands or interests therein taken by the Company under the provisions of the *Expropriation Act* as made applicable to the Company by this Act shall be ascertained in accordance with the provisions of the *Expropriation Act*, and for that purpose the Exchequer Court shall have jurisdiction in all cases relating to or arising out of any such expropriation or taking and

[7] S. of C. 1919, c. 10; R.S.C. 1927, c. 172, s. 17.

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may make rules and regulations governing the institution, by or against the Company, of judicial proceedings and the conduct thereof: Provided that such compensation may, in any case where the offer of the Company does not exceed two thousand five hundred dollars, be ascertained under the provisions of the *Railway Act,* beginning with notice of expropriation to the opposite party. The amount of any judgment shall be payable by the Company.

(3) Lands or interests in lands required by any company comprised in the Canadian National Railways may be acquired for such company by the Company under the provisions of this Act.

The next statute is the one which provides for the works giving rise to the necessity for the lands for which the expropriations in question were effected. It is the *Canadian National Montreal Terminals Act,* 1929.[8] Section 2 of this Act authorizes the Governor in Council to provide for the construction and completion by the Canadian National Railway Company of terminal stations, buildings, tracks, and other works specified in great detail, with "the right to acquire or to take under the provisions of section nine of this Act or otherwise lands and interests in lands for all such purposes, all on the Island of Montreal...or on the mainland adjacent thereto". Section 3 provides for the company raising money by the issuance of securities in respect of the construction and completion of such works, such securities to be guaranteed by the Crown. Section 6 provides for the proceeds of the sale of the securities being held in trust by the Minister of Finance for the company to be released to the company to meet expenditures in connection with the said works, and it also provides that "The said works may be constructed upon property from time to time owned, acquired or taken by the Company", as well as upon property of other companies comprised in the Canadian National Railways such as the Canadian Northern Railway Company and, with the approval of the Governor in Council, "upon property belonging to the Crown". Section 7 provides *inter alia* for the "general plan or plans of the said works" being approved by the Governor in Council. Section 9, which contains the authority for the expropriation in question, then reads as follows:

9. Certain expropriation plans and descriptions heretofore deposited, under the *Expropriation Act,* by or on behalf of the Minister of Railways and Canals for the purposes of the Government Railways having vested in His Majesty lands now required for part of the said works, other plans and descriptions showing lands or interests in lands

[8] Chapter 12 of the Statutes of 1929.

> required or taken from time to time in connection with the said works may be deposited by or on behalf of the said Minister under the *Expropriation Act*. The compensation to be paid in respect of any such taking, subject to the usual right of abandonment as provided in the *Expropriation Act*, may be paid out of the trust funds deposited to the credit of the Minister of Finance under section six of this Act, and upon such payment the lands or interests in lands thereby taken or vested in His Majesty shall upon request be transferred by His Majesty to the Company.

While the provisions prior to section 9 seem to contemplate the works authorized by this Act as being Canadian National Railway Company works, as opposed to Government Railways works, it is to be noted that section 9 refers to certain properties having been expropriated under the *Expropriation Act* "for the purposes of the Government Railways" and now being required for part of the said works, and then provides, and these are the significant words:

> ...other plans and descriptions showing lands or interests in lands required or taken from time to time in connection with the said works may be deposited by or on behalf of the said Minister under the *Expropriation Act*.

Nevertheless, we find that the compensation to be paid in respect of such taking under the *Expropriation Act* is to be paid out of the trust funds raised by securities issued by the Canadian National Railway Company and that, upon such payment, the title in the land is to be transferred by the Crown to the company. It is also of interest to note that section 11 provides that the Minister shall present to Parliament at the beginning of each session "held prior to the completion of the said works" a statement showing the nature and extent of the work done under the authority of the Act, and also provides that the Canadian National Railways shall keep separate accounts of all credits to the trust fund and expenditures made in connection with the said works.

Having reviewed these statutory provisions, I can now turn to the pleadings.

The Information herein, which was filed on November 18, 1957, alleges (paragraph 1) that lands were taken under the *Expropriation Act* by the Crown "for the purposes of a public work of Canada, being the Government Railways" pursuant to the provisions of the *Canadian National Montreal Terminals Act*, 1929, by the deposit of a plan and description with the Registrar of Land in

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Montreal on June 11, 1951, and that such plan and description was signed by the Deputy Minister of Transport. Paragraph 2 alleges that, by virtue of deposit of the said plan and description, the lands in question were vested in the Crown. The Information then goes on to describe a portion of the lands so alleged to have been taken and to say that the defendant claims to have been the owner of the lands so described at the time of the taking by the Crown of such lands. The remainder of the provisions in the Information are irrelevant for the present purposes.

The portions of the statement of defence to which objections are taken read as follows:

> 1. They admit the deposit of the Plan and Description with the Registrar of Land for the Registration Division of Montreal under the No. 898618 on June 11, 1951, referred to in Paragraph 1 of the Information and the said Paragraph 1 is otherwise denied;
>
> 2. Paragraph 2 of the Information filed herein is denied;
>
> * * *
>
> 4. They deny that the lands referred to in Paragraph 4 were taken by the Crown but the Paragraph is otherwise admitted;
>
> * * *
>
> 31. That the lands described in the Statement of Claim, and alleged to have been taken by Her Majesty were not, to their full extent, necessary for the public work contemplated in the Statement of Claim, and Her Majesty has disposed of or shall dispose of at least a portion of the said lands at times when the values of such lands were, or shall be, considerably higher than their value as on June 11th, 1951, the date of the filing of the plan and description in relation to the said lands;
>
> 32. That where lands alleged to have been taken, have been or shall be found to be in excess of the actual requirements of the public work contemplated in the Information, Defendant has a right to the return of such excess of land, or to be compensated therefor in relation to its value at the time of disposal by Her Majesty to other parties, should such value exceed the value of such lands to Defendant on June 11th, 1951, and Defendant estimates the value of such lands over and above the amount claimed in Paragraph 23 of this Defence, on the dates of their subsequent disposal by Her Majesty to be the sum of $1,397,856.83;

Pursuant to order of the Court, on March 13, 1962, the defendant gave "particulars of the defence", and the relevant portions thereof read as follows:

> (A) With respect to paragraphs 1, 2 & 4 of the Defence the Defendant and the Mis-en-Cause state that the basis and the reasons invoked by them for denying in said paragraphs the validity of the expropriation referred to in the present action are that the lands purported to have been taken thereby, or in any event their full extent, were not necessary for the use, construction, maintenance or

repair of a public work of Canada or for obtaining better access thereto, have not been put to such uses nor are they intended to be put to such uses;

* * *

(K) With respect to paragraph 31 of the Defence the Defendant and the Mis-en-Cause state that they are unable to indicate in detail which lands described in the Information and to what extent they are unnecessary for the public work contemplated in the Information nor which lands the Plaintiff will dispose of or when such disposition has been or will be made, since neither the Defendant nor the Mis-en-Cause are privy to the plans of Plaintiff in this regard. However, the Defendant and the Mis-en-Cause rest their contentions with respect to such allegations contained in paragraph 31 upon the fact that no commencement has been made by the Plaintiff or those for whom it acts upon the public work alleged to have necessitated the expropriation within the lengthy period which has intervened between the date of the expropriation and the present, nor has there been any indication that such works are to be commenced, and the Defendant and the Mis-en-Cause can only conclude that the vast expense (*sic*) of land area expropriated will be devoted to purposes other than those for which the expropriation is alleged to have been necessary;

* * *

(L) With respect to paragraph 32 of the Defence the Defendant and the Mis-en-Cause state that they are unable to know which of such lands will be found to be in excess of actual requirements nor when such determination shall be made since these are matters solely within the knowledge of the Plaintiff or those for whom she acts and such knowledge has not been imparted by the Plaintiff to Defendant and the Mis-en-Cause. Defendant and the Mis-en-Cause have, therefore, no choice but to assume that all lands purported to have been taken shall be found to be not required for the purpose stated in the Information and to claim an additional sum equal to an estimated increase in value in the said lands between the date of the expropriation and the date of the disposal of such lands by the Plaintiff to persons other than Defendant or the Mis-en-Cause. The Defendant and the Mis-en-Cause have, therefore, estimated such increase of value at a uniform rate of .50 per square foot for all lands purported to have been taken and have calculated the said sum of $1,397,856.83 on such basis.

As I read these various provisions in the statement of defence, and the particulars that are under attack, they are based exclusively on the view that it can be established that the lands that are the subject matter of the expropriation, or at least some part of such lands, were "unnecessary" for the "public work contemplated in the Information". They do not allege that the lands were taken for some work other than one falling within the relevant expropriating authority.

I turn now to consider what was decided in *Boland v. Canadian National Railway Co.*, the decision of the Privy Council to which I have already referred. In that case the

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Canadian National Railway Company had filed a plan and description under the *Expropriation Act* pursuant to section 13 of the *Canadian National Railway Act* of 1919 for a parcel of land that was required to construct a roadway to give certain premises access to a subway under the railway that was being constructed pursuant to an order of the Railway Board of Canada, and the validity of the expropriation was attacked by the owner of the land in question. The Privy Council held that the proposed roadway for which the lands were taken was no part of the railway undertaking but was part of the municipal road system, and that the expropriation was not, therefore, authorized by the *Canadian National Railway Act* of 1919. In disposing of this branch of the case, Viscount Dunedin makes a reference to section 11 of the then *Expropriation Act* which is the same as section 12 of the present *Expropriation Act,* in a passage that reads as follows:

> Their Lordships are, therefore, of opinion that the ground of judgment of Orde J. fails. It is, of course, not open to any judicial tribunal to question the wisdom of the legislature when the terms of the legislation are explicit, but in order to aid construction it is legitimate to look at the opposing contentions. If Orde J.'s views were right the result would be very astounding. The railway authorities would have the right to take any land anywhere for any purpose whatever, and with the immunity from giving explanation afforded by s. 11 they could requisition lands which had no connection with the undertaking, and they might proceed to dispose of them or use them as they pleased.

As I understand this decision, it means that the Court must consider an attack on an expropriation based upon an allegation that the work for which the land was taken is not a work for which the expropriating authority was authorized to take land. It does not say that section 12 must not be given full force where the work does fall within the expropriating authority, but there is an attack based on an allegation that the land taken or some part of it is not necessary for that work. In any event O'Connor J., giving the judgment of this Court in *The King v. City of Toronto,*[9] held, after considering the Privy Council decision, that section 12 operated to require that "the filing of the plan shall be deemed to indicate that in the Minister's judgment the land is necessary for the purpose of a public work", and that "his judgment is not open to review by the Court by reason of section 12", and I adopt his view of

[9] [1946] Ex. C.R. 424.

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the effect of that section. Even apart from his decision, I should have thought I would reach the same conclusion. Compare *Calgary Power Ltd. v. Copithorne*[10].

I am therefore of the view that the defences to which objection have been taken are not open to the defendant and that the offending provisions of the statement of defence and of the Particulars should be struck out.

There is, however, a matter to which I referred earlier with which I must deal. Counsel for the defendant indicated that it had been the intention in making the pleas that I have decided to strike out, to raise, not only the attack based on the necessity of the land taken for the works in question, but also to raise a contention that the lands in question were not for works included in a "general plan or plans of the said works" that had been approved by the Governor in Council as was required by section 7 of the *Canadian National Railway Montreal Terminals Act*. The order will be, therefore, that the portions of the statement of defence and the particulars in question are struck out and that the defendant has leave to substitute therefor an appropriate pleading, which must be satisfactory to the Court, raising the defence under section 7.

Finally, I should say that counsel for the defendant also urged that, even if my decision is against him on the main question, the latter part of paragraph 31 of the statement of defence should be allowed to stand. That part reads as follows:

> ...Her Majesty has disposed of or shall dispose of at least a portion of the said lands at times when the values of such lands were, or shall be, considerably higher than their value as on June 11th, 1951, the date of the filing of the plan and description in relation to the said lands;

Counsel was not able to suggest to me any view upon which this allegation would be an allegation of a material fact even if it is a fact that might be admissible as evidence. (Compare Rule 88 of the Exchequer Court Rules.) I must, therefore, refuse to accede to this submission.

When counsel have had an opportunity to consider the terms of an order to implement these conclusions, I will pronounce my order after hearing what they have to say. Costs of the application will be to the plaintiff in any event of the cause.

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[10] [1959] S.C.R. 24.

Ottawa 1968 June 27 — July 16

BETWEEN:

THE JOHN BERTRAM AND SONS COMPANY LIMITED .... SUPPLIANT;

AND

HER MAJESTY THE QUEEN ....RESPONDENT.

Courts—Judicial comity—Decision of Supreme Court of Ontario construing contract re liability for federal sales tax—Subsequent claim for refund of sales tax—Whether Exchequer Court bound by decision—Res judicata—Stare decisis.

By a contract made in April 1963 governed by the laws of Ontario suppliant agreed to sell a planetary mill to another company for $5,100,000 subject to adjustment for any federal sales tax imposed by law. Such mills became subject to federal sales tax under a statute (S. of C. 1963, c. 12) which contained a saving clause for a mill sold under a contract signed before 14th June 1963 if such contract did not permit the tax to be passed on to the purchaser. Suppliant paid sales tax of $451,735 under protest. The purchaser then applied to the Supreme Court of Ontario for construction of the contract and that court (Landreville J) after hearing full argument held that under the contract suppliant was liable for the tax. Suppliant then demanded refund of the tax paid.

Held, suppliant was entitled to the refund. While the judgment of the Ontario court was not *res judicata* since the Queen was not party to the proceedings in that court, nor did the principle of *stare decisis* require this court to follow the decision of another court of co-ordinate jurisdiction, nevertheless judicial comity required that this court follow the judgment of the Ontario court in the absence of a strong reason to the contrary; the fact that this court would not have construed the contract as Landreville J. had done was not a sufficient reason.

Canada Steamship Lines Ltd. v. M.N.R. [1966] C.T.C. 255; *R. v. Northern Electric Co.* [1955] 3 D.L R. 449; *Woods Mfg. Co. v. King* [1951] 2 D.L.R. 465, referred to.

PETITION OF RIGHT.

Gordon F. Henderson, Q.C. and *Brian A. Crane* for suppliant.

Derek H. Aylen and *J. E. Smith* for respondent.

CATTANACH J.:—The suppliant, by its petition of right, seeks to recover from the respondent the sum of $451,735.48 paid by it to the Receiver General of Canada on three divers dates in the years 1965 and 1966 by way of sales tax under the *Excise Tax Act*[1] as amended, upon the sale of one Sendzimir type planetary hot mill pursuant to a

[1] R S.C. 1952, c. 100.

written agreement made on April 15, 1963, between the suppliant and Atlas Steels Company, a division of Rio Algom Mines Limited, for a purchase price of $5,150,000, subject to change for causes set out in the agreement, together with interest at the rate of 5 per cent per annum on the amount so paid to the Receiver General from the three respective dates of payment.

The suppliant seeks to recover the sum so paid, by way of a refund or deduction of tax pursuant to section 10 of chapter 12 of the Statutes of Canada 1963 being an Act to amend the *Excise Tax Act.* Prior to the enactment of this amendment the mill, which fell under the heading of "Machinery and Apparatus to be Used in Manufacture or Production" in Schedule III of the *Excise Tax Act,* had been exempt from federal sales tax. By virtue of section 7(6) of this amendment all that portion of Schedule III under the immediately foregoing heading was repealed so that the mill so sold was made subject to the federal sales tax.

However, section 10 of the foregoing amendment (the pertinent portion of which is reproduced in the footnote hereunder)[2] provided that where any tax has become payable in respect of designated goods that were, not later than December 31, 1964, sold and delivered pursuant to a "*bona fide*" contract in writing that provided for the sale of those goods for a fixed amount stated in the contract

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[2] 10. (1) Where any tax under Part VI of the *Excise Tax Act* has become payable by any person in respect of any designated goods that were, not later than December 31, 1964, sold and delivered by that person, or applied by that person to a use resulting in the property in the goods passing from that person, pursuant to a *bona fide* contract in writing

(*a*) that provided for the sale of those goods or their application to that use for a fixed amount stated in the contract and that did not permit the adding of the tax to the amount payable to that person under the contract, and

(*b*) that was signed by the parties thereto

(i) on or before June 13, 1963,

. . .

a refund, or deduction from any of the taxes imposed by the said Act, of the tax or such part thereof as could not under the contract be added to the amount payable to that person thereunder may, where application therefor is made to the Minister of National Revenue by that person within two years from the time the goods were delivered by that person or applied by him to that use, be granted to that person

. . .

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and that did not permit the adding of the tax to the amount payable to the taxpayer under the contract, and that was signed by the parties thereto on or before June 13, 1963, a refund or deduction from any of the taxes imposed by the said Act of the tax or such part thereof as could not under the contract be added to the amount payable to the taxpayer thereunder may, where application therefor is made to the Minister of National Revenue by the taxpayer, within two years from the time the goods were delivered by the taxpayer, be granted to the taxpayer.

There is no dispute between the parties hereto that the mill here in question fell within the category of "designated goods" within the meaning of those words as they appear in section 10 of the statute amending the *Excise Tax Act,* nor that the mill was sold and delivered prior to December 31, 1964, pursuant to a written contract signed by the parties thereto prior to June 13, 1963. Neither is it disputed that the three amounts were paid by the suppliant under protest since the suppliant maintained that it fell within the precise terms of the exemption outlined in section 10 and that the tax was paid by the suppliant to avoid penalties being assessed against it if the tax were not paid. It is also agreed between the parties that the suppliant made application to the Minister of National Revenue for refund of the tax paid within the time prescribed in the statute.

The sole controversy between the suppliant and the officials of the Department of National Revenue was whether, under the terms of the written contract dated April 15, 1963 between the suppliant as vendor of the mill and Atlas Steels Company as purchaser, the suppliant was permitted thereby to add the amount of the tax imposed to the amount payable by the purchaser under that contract. Obviously the officials of the Department were adamant in their opinion that the contract between the contracting parties did permit the tax to be passed on to the purchaser while the suppliant was equally adamant that the contract with its purchaser did not so permit.

Prior to trial the parties agreed upon a statement of facts as follows:

1. The Suppliant (hereinafter referred to as "Bertram"), a corporation incorporated pursuant to the laws of Canada, having its head office in the Town of Dundas, in the Province of Ontario, entered into a bona fide contract in writing with Atlas Steels Company

(hereinafter referred to as "Atlas"), a division of Rio Algom Mines Limited, which contract was signed by the parties thereto on or about the 15th day of April, 1963, whereby Bertram agreed to sell and Atlas agreed to purchase a certain Sendzimir planetary hot mill for the sum of $5,150,000 00, subject to the terms and conditions of the said contract, a copy of which is attached hereto as

Appendix "A"

2. The aforesaid contract in writing was prepared by Atlas. At the time it was made Atlas and Bertram had manufacturers' licences issued under Section 34 of the *Excise Tax Act* and were making returns to the Department of National Revenue and paying sales tax on taxable articles.

3. Attached hereto and marked *Appendix "B"* is a letter from Atlas to Bertram dated December 31st, 1964 delivered to the addressee on the same date. The payments referred to therein were made to Bertram on the due dates.

4. The terms and conditions of the said contract required that the said mill components be delivered not later than the 15th day of October, 1964, and manufacture and delivery of the said mill, pursuant to the said contract, was completed on or before the 31st day of December, 1964.

5. The said mill was "Machinery and Apparatus to be Used in Manufacture or Production" within the meaning of Schedule III of the *Excise Tax Act,* R S C. 1952, Chapter 100, as amended by Section 2 of 1960, Statutes of Canada, Chapter 30, and was exempt under that heading from sales tax under Part VI of the *Excise Tax Act*. The said heading and all that portion of the Schedule under the said heading as previously enacted by Section 2 of 1960, Statutes of Canada, Chapter 30 was repealed by Section 7, subsection (6) of the 1963 Statutes of Canada Chapter 12, which provision was deemed to have come into force on June 14th, 1963, and sales tax under Part VI of the *Excise Tax Act* therefore became payable in respect of the said mill.

6. By instalments of $340,000 00 paid on the 1st day of February, 1965, and of $64,770 65 paid on the 3rd day of August, 1965 and of $46,964 83 paid on the 25th day of April, 1966, Bertram paid the sum of $451,735 48 to the Receiver General of Canada as Sales Tax imposed under Part VI of the *Excise Tax Act* in respect of the sale of the said mill. Each of the instalments of tax as aforesaid was paid "under protest".

7. By motion brought on the 15th day of June, 1965, and argued on the 28th day of June, 1965, the Supreme Court of Ontario was moved, pursuant to Rules 611 and 612 of the Rules of Practice of that Court under the *Ontario Judicature Act,* R S O 1960, Chapter 197, as amended, by counsel for Atlas to determine and declare the rights of Bertram and of Atlas under the said contract, and in particular to determine and declare whether the liability, if any, to pay a certain Federal Sales Tax imposed by the *Excise Tax Act* rested upon Atlas or upon Bertram. Judgment upon the said application was reserved, and subsequently by order of the Supreme Court dated the 2nd day of July, 1965, it was ordered that: "...the liability, if any, to pay a certain Federal Sales Tax imposed by the *Excise Tax Act* of 1952, Revised Statutes of Canada, Chapter 100, as amended, rests upon The John Bertram and Sons Company Limited having

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regard to the provisions of an Agreement dated the 15th day of April, 1963 made between Atlas Steels Company and The John Bertram and Sons Company Limited..." Copies of the Notice of Motion, Affidavit of Harry Scott Wilson in support (the exhibit thereto is *Appendix "A"*), formal Order and Reasons for Judgment in the said application are attached hereto and marked *Appendix "C"*.

8. By letters addressed to the Deputy Minister of National Revenue for Customs and Excise dated the 16th day of September, 1965, the 7th day of January, 1966, and the 20th day of January, 1967, Bertram applied for a refund of the aforementioned sum paid as sales tax, pursuant to the provisions of subsection (1) of Section 10 of 1963, Statutes of Canada, Chapter 12, on the grounds set out in the letters. Copies of the said letters are attached hereto and marked *Appendix "D"*.

By letter dated the 13th day of December, 1965 the Deputy Minister of Revenue for Customs and Excise denied the request of Bertram for the said refund. A copy of the said letter is attached hereto and marked *Appendix "E"*.

9. By letter dated the 14th day of September, 1966 Bertram applied to the Tariff Board pursuant to Section 57 of the *Excise Tax Act* for a declaration of the board that no sales tax pursuant to Part VI of the *Excise Tax Act* was payable in respect of the sale and delivery of the said mill by Bertram to Atlas and for a further declaration that a refund of the said tax paid be made to Bertram. On or about the 6th day of March, 1967 the Tariff Board held that it did not have jurisdiction under Section 57 of the *Excise Tax Act* to make a declaration in this matter, and accordingly dismissed the application for lack of jurisdiction. A copy of the Reasons for Judgment of the Tariff Board are attached hereto and marked *Appendix "F"*.

10. The following Statement of Facts is hereby agreed to on behalf of the Suppliant, The John Bertram and Sons Company Limited, and the Respondent, for the purpose of enabling the Exchequer Court of Canada to hear and consider the Suppliant's petition for a declaration that the Suppliant is entitled to have refunded to it the sum of $451,735.48, together with interest thereon at the rate of 5% per annum from the date of payment thereof.

Appendix "A" to the agreed statement of facts is a photostatic copy of the contract dated April 15, 1963 between the suppliant and Atlas Steels Company which contract was prepared by Atlas Steels Company.

Paragraph 15 of that contract sets out the purchase price of the mill as $5,150,000 with the stipulation that "This price is not subject to escalation or change for any cause except as set forth in paragraph 18".

Paragraph 18 referred to in paragraph 15 is headed "Price Adjustment" and reads as follows:

> The price for the Mill shall be subject to the following adjustment:
>
> (*a*) the amount of any Federal or Provincial Sales Tax imposed by law;

(b) the amount of any increase or decrease resulting from changes required by Atlas under paragraph 8(c); and
(c) charges for installation services under paragraph 19;
(d) penalty and bonus adjustments under paragraph 6.

Paragraph 17 provides for the terms of payment and paragraph 23 provides that the agreement shall be governed by and interpreted in accordance with the laws of the Province of Ontario, but the question whether the suppliant as vendor may add the tax to the purchase price payable by the purchaser and so qualify for a refund of (or in effect exemption from) sales tax is dependent upon the interpretation of paragraph 18(a) set out above.

Appendix "B" is a photostatic copy of a letter dated December 31, 1964 written by Rio Algom Mines Limited (the effective purchaser of the mill) to the suppliant denying its liability in respect of federal sales tax demand for the payment of which had been made by the suppliant.

Despite its denial of liability Rio Algom Mines Limited paid to the suppliant the amount of the sales tax demanded but subject to the conditions that,

(1) the payment was made under protest,
(2) the suppliant remit the tax to the Department of National Revenue under protest and making known the purchaser's protest, and
(3) judicial proceedings be taken to resolve the rights of the contracting parties in respect of federal sales tax under the contract of April 15, 1963 between them.

It was also agreed and understood that if the judicial interpretation of the contract resulted in a refund of the sales tax to the suppliant, that the amount of such refund would be promptly refunded by the suppliant to the purchaser.

As outlined in paragraph 7 of the Agreed Statement of Facts, a motion was brought on June 15, 1965 and argued on June 28, 1965, before the Supreme Court of Ontario pursuant to Rules 611 and 612 of the Rules of Practice of that Court to determine and declare the rights of the parties to the contract of sale under their contract and in particular whether the liability, if any, to pay the federal sales tax fell upon the purchaser, Atlas Steels Company, or upon the vendor, the suppliant herein.

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Appendix "C" to the Agreed Statement of Facts is a copy of the Notice of Motion dated June 15, 1965, the formal Order dated July 2, 1965 and the Reasons for Judgment.

The pertinent language of the Order reads as follows:

> 1. THIS COURT DOTH DECLARE that the liability, if any, to pay a certain Federal Sales Tax imposed by the *Excise Tax Act* of 1952, Revised Statutes of Canada, ch. 100, as amended, rests upon The John Bertram and Sons Company Limited having regard to the provisions of an Agreement dated the 15th day of April, 1963 made between Atlas Steels Company and The John Bertram and Sons Company Limited,...[3]

In the Reasons for Judgment also delivered on July 2, 1965, Landreville J. stated:

> ...After reading the contract as a whole and more particularly the above-numbered clauses (i.e. clauses 15, 17 and 18) I have come to the conclusion that the contract, while referring to the sales tax, does not specifically and clearly state who is to pay same Due to the fact that the statute which subsequently came into existence imposes on the manufacturer the tax, it is not that clear language necessary for me to displace the obligation to the purchaser.
>
> I accept the argument of the applicant that the words imposed "by law" make reference and contemplate the tax which might be in existence at that time. I understand that the goods manufactured could have been pleaded to have been exempted from taxation at the time of contract.
>
> Not knowing on whom to place the responsibility for the loose wording of the contract, there will be no taxable costs on this motion.

Appendix "D" to the Agreed Statement of Facts is comprised of three letters written by the suppliant to the Department of National Revenue.

The first letter is dated September 16, 1965 and was an application for a refund of the tax paid. It recapitulated the dispute between the suppliant and the Departmental officials setting out that the Department's view that the contract of April 15, 1963, was not within the exemption contemplated by section 10 of the amending statute and the suppliants disagreement with that view. The letter referred to the proceedings taken before the Supreme Court of Ontario pointing out that the Court arrived at a

[3] While this judgment merely declares what the *Excise Tax Act* clearly provides which is that the sales tax shall be paid by the manufacturer, nevertheless both counsel argued the present matter accepting that the true purport of this judgment as deciding that the manufacturer having paid the tax, the contract between the manufacturer and purchaser did not permit the adding of the tax to the purchase price and I have discussed the matter on that basis.

conclusion opposite to that of the Department and had held that the suppliant could not pass on the tax to its purchaser under the contract between them. The letter continued to the effect that since the suppliant's rights as against the purchaser had been judicially determined adversely to the suppliant, the question had been determined by the Court having jurisdiction and so the contract fell expressly within section 10 of the Act amending the *Excise Tax Act*. Copies of the pertinent Court Order and Reasons for Judgment were enclosed.

The second letter in Appendix "D" is dated January 7, 1966, acknowledging a departmental letter of December 17, 1965. It states in part:

> ...As a result of that letter, Bertram finds itself in a very difficult situation, since the Supreme Court of Ontario has explicitly stated that the contract in question does not permit the tax to be added to the purchase price, while your solicitors appear to have taken a position which is directly in conflict with the order of the Ontario Court.
>
> . . .

Parenthetically speaking, I have some reservations as to the difficulty to which the suppliant refers to as finding itself in, bearing in mind the letter dated December 31, 1964, from Rio Algom Mines Limited to the suppliant, Appendix "B", refers to the circumstance that if the judicial interpretation sought should result in a refund of any sales tax under the contract, then the purchaser expects a refund forthwith. The judicial interpretation obtained did not result in the Department of National Revenue changing its attitude and no refund was forthcoming. The attitude of Rio Algom Mines Limited expressed in its letter of December 31, 1964, appears to be to the effect that it did not expect a refund of the tax paid to the suppliant under protest unless a refund was forthcoming from the Department to the suppliant from which it seems to follow that Rio Algom Mines Limited would assume the responsibility for the payment of the tax. However, it might be that following the decision of the Supreme Court of Ontario that the purchaser was not liable to the suppliant for the sales tax imposed and which decision determined the rights between those parties, Rio Algom Mines Limited changed its attitude and expects the suppliant to refund to it the amount so paid in any event. If such is the case then the

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suppliant's difficulty is readily apparent, but there has been no evidence to this effect and I do not think that this circumstance is material to the question I have to decide.

The third letter in Appendix "D" is from the suppliant to the Department of National Revenue dated January 20, 1967, enclosing a further payment of sales tax and simultaneously requesting its refund.

Appendix "E" is a letter dated December 13, 1965, from the Department of National Revenue to the suppliant, and which was written subsequent to the Order of the Supreme Court of Ontario dated July 2, 1965, (Appendix "C"). The pertinent part of this letter reads as follows:

> . . .
>
> I now have an opinion from the Department of Justice in this matter and it is the view of our Solicitors that the contract in question permits the tax to be added to the purchase price. This, in fact, has been done and, consequently, the refund that you are seeking cannot be approved.

Obviously, so far as the Department of National Revenue is concerned, the matter is concluded and the Department has decided that the requested refund of the sales tax collected from the suppliant would not be made to it.

Thereupon the suppliant applied to the Tariff Board pursuant to section 57 of the *Excise Tax Act* for a declaration that no sales tax was payable on the sale of the mill by the suppliant and that a refund of the tax paid be ordered to be made to the suppliant. The Tariff Board dismissed the appeal for lack of jurisdiction. Appendix "F" to the Agreed Statement of Facts is a copy of the Board's Reasons for Judgment.

At the trial counsel introduced as Exhibit 2, a photostatic copy of a letter dated January 29, 1965, written by the suppliant to the Department of National Revenue. In this letter the suppliant forwarded the amount of $340,000 as part payment of the sales tax. The suppliant did so under protest maintaining that no tax was owing and that it did so to prevent penalty interest arising if it should ultimately be determined that the tax was properly exigible. The letter also referred to the opinion of the officials of the Department of National Revenue that the contract for the sale of the steel mill dated April 15, 1963, between the suppliant and its purchaser which gives rise to the disputed amount was not a contract which qualified the suppliant for relief under section 10 of the 1963 amendments to the *Excise Tax Act*. The suppliant then stated in its letter that it intended to seek judicial interpretation in the Ontario Courts as to whether, under the terms of that contract, the suppliant had the right to pass on to Atlas Steels Company (the purchaser) the burden of sales tax imposed by the amendment to the *Excise Tax Act*, effective June 13, 1963. The letter concluded with the statement that if the result of such a determination should be that the suppliant did not have the right to demand payment of the sales tax from its purchaser that the suppliant then intended to apply for a refund of the amount paid and any subsequent payments similarly made by it.

There was no other evidence adduced.

As I have intimated before, the question which I must decide is whether the suppliant is entitled to a refund of the sales tax paid by it under the *Excise Tax Act* by virtue of section 10 of the Act to amend the *Excise Tax Act*, 1963 Statute of Canada, chapter 12. All essential elements required by section 10 to entitle the suppliant to a refund are present with one possible exception, which is the subject matter of the dispute between the parties hereto, and that is whether or not the contract of April 15, 1963, between the suppliant and Atlas Steels Company for the sale of a steel mill permits the suppliant to add the tax to the purchase price payable by the purchaser. If the language of the contract so permits, then the suppliant is not entitled to the refund it seeks, but if it cannot add the tax to the purchase price under the contract of sale, then the suppliant is entitled to the refund.

To reach that decision I must consider the contract to ascertain whether or not the suppliant is entitled to pass the tax on to the purchaser. Therefore the meaning of the contract, normally to be determined from the language employed in the contract itself, is vital to the determination of the issue herein.

Counsel for the suppliant submitted that I am absolved from interpreting the meaning of the contract because that has already been done for me in an adversary proceeding between the parties to the contract before the Supreme Court of Ontario, which is the Court having jurisdiction to determine the rights between those parties. With the

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proposition that the Supreme Court of Ontario is the Court having jurisdiction to determine the rights as between the parties to the contract and that its decision is binding on those parties, I am in complete accord. At one stage in the course of his argument counsel for the suppliant suggested that it was very debatable whether I had jurisdiction to consider the contract even collatorally to the issue which I must decide and that the only Court competent to interpret the contract would be the court having jurisdiction over the parties to the contract, which in the present instance would be the Ontario Court. In the circumstances of the present action, I am not called upon to decide that matter and accordingly do not comment thereon except to say that I have difficulty in appreciating how this Court can discharge its judicial functions if that be the law.

The only principles of which I know under which the judgment of the Supreme Court of Ontario might be binding upon me are those commonly called *res judicata* and *stare decisis*.

A decision as to a right, question, or fact distinctly put in issue, as was the interpretation of the contract of April 15, 1963, between the suppliant and Atlas Steels Company, and which was directly determined by the Supreme Court of Ontario, a Court of competent jurisdiction, cannot be disputed in a subsequent suit between the same parties. Even if the subsequent suit is for a different cause of action, the right, question or fact once so determined must, as between the parties, be taken as conclusively established so long as the judgment in the first suit remains unmodified. An adjudicated matter is forever binding between the parties.

It was suggested, during argument, that the respondent had ample notice of the impending action before the Supreme Court of Ontario so that it could have applied to become a party thereto. On the other hand there was some question whether the respondent was entitled to be joined under the Rules of Practice of the Supreme Court of Ontario. However I consider such circumstances to be immaterial to the decision of the question before me. The simple fact is that the respondent was not a party to the proceedings before the Supreme Court of Ontario and its decision did not resolve the issue between the suppliant and the respondent.

For the reason that the respondent was not a party to the action in which the judgment of Landreville J. was given the doctrine of *res judicata* cannot be here invoked, nor does counsel for the suppliant invoke it.

Neither does he seek to invoke the principle of *stare decisis*. One of the most elusive areas of the doctrine of precedent has been the respect to be accorded by a single judge to the opinion of another judge of equal jurisdiction. The view expressed in Halsbury[4] is that there is no common law rule compelling one court to abide by the decision of another court of co-ordinate jurisdiction. Therefore I am not bound by the decision of Landreville J.

The argument of counsel for the suppliant, as I understood it, was threefold.

First he submitted that the judgment of Landreville J. is the fact which determines the rights between the parties to that action and that the refund under section 10 of the Act to amend the *Excise Tax Act* depends upon the rights as between those parties as so determined. In other words he says that section 10 must be interpreted in the light of the fact that the suppliant has been found not to be entitled to pass the sales tax on to the purchaser under the contract between them by a court having the jurisdiction to so determine in a non-collusive adversary action before it. He went on to say that the judgment of Landreville J. is conclusive of the fact that the incidence of the tax falls on the vendor from which it follows that the refund must be forthcoming to the suppliant from the respondent.

Because of the view I take of the matter, it is not necessary for me to express an opinion on this submission.

Secondly counsel for the suppliant submitted that even if the decision of the Provincial court is not determinative and conclusive of a material fact this Court should abide by the decision of another court of co-ordinate jurisdiction, not because of the principle of *stare decisis*, but because of judicial comity.

Thirdly, he submitted that the interpretation of the contract by Landreville J. was right in any event.

[4] 3rd. ed. 1958, vol. 22, pp. 801-802.

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With respect to the third submission on behalf of the suppliant, I must say that if the matter had come before me initially, untrammelled by the judgment of Landreville J., I would have come to a conclusion contrary to his. Considering the contract as a whole and what I conceive to be the fair and plain meaning of the language of paragraph 18(*a*) thereof, I would have concluded that the parties thereto contemplated that any federal sales tax imposed by law would be the subject matter of a price adjustment to be borne by the purchaser.

At the time the contract for the sale of the steel mill was signed by the parties thereto, the mill was exempt from any federal sales tax whatsoever. However in accordance with the contract, the mill would not have been delivered until approximately a year later and because of that interval in time it is inconceivable to me that the parties were oblivious of the possibility that a federal sales tax might be imposed prior to delivery of the mill. If such were not the case it would not have been necessary to include a paragraph such as 18(*a*) in the contract. The obvious purpose of paragraph 18 is to provide against contingencies and uncertainties and, in my view, the imposition of a federal sales tax was such a contingency provided against. By paragraph 15 the purchase price was a specified amount not subject to escalation or change for any cause except as outlined in paragraph 18. Since the mill was exempt from tax at that time the only possible change that could have been contemplated by the parties would be an increase in the purchase price consequent upon the imposition of a federal sales tax. It could not be a decrease but only an escalation.

Paragraph 18 is headed "Price Adjustment" and for convenience I repeat the language of 18(*a*) here.

> The price for the Mill shall be subject to the following adjustments:
>
> (*a*) the amount of any Federal or Provincial sales tax imposed by law;

I cannot agree with Landreville J. that "the words imposed 'by law' make reference and contemplate the tax which might be in existence at that time". First, because there was no federal sales tax imposed by law at that time, secondly, because the words "imposed by law" is the adjectival use of a participle modifying the word "tax" and thirdly, because of the inclusion of the word "any". It accordingly seems clear to me that the language employed contemplates a possible future tax being borne by the purchaser by way of an increased price.

However this Court has generally taken the position that judgments of courts of equal or co-ordinate jurisdiction should be followed in the absence of strong reasons to the contrary.

In *Canada Steamship Lines Ltd. v. M.N.R.*[5] the President of this Court did not feel himself free to consider an approach to the disposition of the problem there before him different from the approach adopted in two previous decisions by other judges of this Court. He said at page 259:

> ...I think I am bound to approach the matter in the same way as the similar problem was approached in each of these cases until such time, if any, as a different course is indicated by a higher Court. When I say bound, I do not mean that I am bound by any strict rule of *stare decisis* but by my own view as to the desirability of having the decisions of this Court follow a consistent course as far as possible.

While I fully appreciate that the President was addressing his remarks to decisions of other judges of the same Court, nevertheless, I believe that his remarks apply with equal force to the decisions of another court of co-ordinate jurisdiction.

In considering what "strong reason" would justify a departure from a decision of a judge of the same Court or of a court of co-ordinate jurisdiction, McRuer, C.J. H.C. had this to say in *R. v. Northern Electric Co.*[6]:

> I think that "strong reason to the contrary" does not mean a strong argumentative reason appealing to the particular judge, but something that may indicate that the prior decision was given without consideration of a statute or some authority that ought to have been followed. I do not think "strong reason to the contrary" is to be construed according to the flexibility of the mind of the particular judge.

Landreville J. reached his decision after the matter was fully argued before him and to which arguments he had given mature consideration. His decision was not *per incuriam* nor was it the result of any slip or inadvertence. So far as I can see no additional or different evidence was adduced before me, nor was any authority cited to me of

[5] [1966] C.T.C. 255.

[6] [1955] 3 D.L.R. 449 at 466.

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which Landreville J. was not aware. Therefore there is no compelling reason for me to depart from his decision that under the terms of its contract the suppliant was liable to pay the federal sales tax imposed by the *Excise Tax Act* and could not thereunder be reimbursed by its purchaser by way of increased purchase price even though I might well have reached a different conclusion if the matter had come before me originally for the reasons I have outlined above. I accept his conclusion with the realization that I am not bound to abide by it upon the rule of *stare decisis* but rather upon what Brett M.R. described in the *Vera Cruz*[7] as "comity among judges". Such adherence is most advantageous for without it the administration of justice would become disordered, the law would become uncertain and the confidence of the public undermined. (In so stating I am adopting the language of Rinfret, C.J.C. in *Woods Mfg. Co. v. King*[8], commenting on the benefits of the principle of *stare decisis* which comments I believe to be applicable to judicial comity as well.)

It therefore follows that the suppliant is entitled to have refunded to it the sum of $451,735.48.

There remains the question whether the suppliant is entitled to interest at the rate of 5 per cent per annum on $340,000 paid by it on February 1, 1965, $64,770.65 paid by it on August 3, 1965 and $46,964.83 paid by it on April 25, 1966, from those respective dates to the date of judgment herein as prayed for in its petition of right. Section 10 of the Act to amend the *Excise Tax Act* contemplates a refund of the tax paid where an applicant complies with the requirements therein outlined. There is no reference to interest being payable on such refund. I am aware of no other statutory enactment, nor was any cited to me, which would authorize the payment of interest. Accordingly in the absence of statutory authority I do not feel justified in purporting to exercise a discretion by ordering the payment of interest.

The suppliant is therefore entitled to recover from Her Majesty the Queen the sum of $451,735.48 being part of the relief sought by its petition of right herein, and costs to be taxed.

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[7] (1884) 9 P.D. 96 at 98.

[8] [1949] Ex. C.R. 9; [1951] 2 D.L.R. 465 at 471.

BETWEEN:

Ottawa
1968

July 11

July 17

THERAPEUTIC RESEARCH CORPORATION LIMITED, LOTHAR MICZKA AND LOTHAR MICZKA K.G. .... PLAINTIFFS;

AND

LIFE AID PRODUCTS LIMITED .... DEFENDANT.

Trade marks—Photographs of another's product with substituted label—Contrary to honest commercial usage—Trade Marks Act, s. 7(e)—Interlocutory injunction.

Pending completion of a prototype of its own oxygen mask defendant published a leaflet containing photographs of plaintiffs' oxygen mask with defendant's label replacing plaintiffs'.

Held, plaintiffs were entitled to an interlocutory injunction. In falsely representing as its own a device which was plaintiffs' and which moreover differed from its own defendant deceived the public and acted contrary to honest industrial or commercial usage in Canada within the prohibition of s. 7(*e*) of the *Trade Marks Act.*

APPLICATION.

George A. Rolston for plaintiffs.

D. S. Johnson, Q.C. for defendant.

NOËL J.:—This is an application for an interlocutory injunction restraining the defendant until the trial or other disposition of this action from (a) defacing, covering, concealing or altering the labelling applied to plaintiffs' breathing devices; (b) printing, publishing or in any way making use of photographs or photographic illustrations of oxygen breathing devices manufactured or sold by one or other of the plaintiffs; (c) from making any written pictorial or verbal representations or suggestions to the trade or to the public tending to suggest that the oxygen breathing devices manufactured, imported and/or sold by one or other of the plaintiffs are manufactured and/or sold by the defendant or that any patent rights or rights in any patent application in relation to or in respect of or concerning the oxygen breathing device of the plaintiffs are owned by or

*Leave to appeal this decision to the Supreme Court of Canada was refused.

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will be owned or obtained by the defendant or any person other than the first plaintiff. The application further requests:

(h) an order under rule 148(*a*) of the Rules of the Exchequer Court that the Defendant do forthwith deliver up to the Registrar of this Honourable Court for detention and preservation until trial or other disposition of this action the oxygen breathing device demonstrated to the said M Neiman in April 1968 by the Defendant at 86 Bloor Street West, City of Toronto, Province of Ontario, Canada.

(i) an order under Rule 148(*a*) of the Rules of the Exchequer Court directing the Defendant to permit inspection by the Plaintiffs and their Counsel of all prototype oxygen breathing devices in the possession, power or control of the Defendant and either manufactured by the third Plaintiff, designed by the second Plaintiff, or obtained from the first Plaintiff, and further directing the Defendant to permit inspection by the Plaintiffs and their Counsel of the original photographs and photographic negatives from which the photographic illustrations appearing in the said leaflet of the Defendant referred to in the Statement of Claim herein were prepared, and further granting the Plaintiffs leave to conduct experiments and to make observations in respect of the articles so inspected for the purpose of obtaining full information and evidence therefrom.

(j) and for such further or other order as this Honourable Court shall seem meet.

There are no patents issued or industrial design or trade mark registered by any of the plaintiffs although there are applications pending for this device of which it is alleged plaintiff Lothar Miczka is the inventor and author, Lothar Miczka K.G. is the manufacturer and Therapeutic Research Corporation Limited, a Canadian corporation, the assignee of the exclusive Canadian rights.

A leaflet put out by the defendant corporation, Exhibit MN 5, gave rise to the present proceedings by depicting thereon, by means of five photographs, an oxygen mask which the defendant states to be its product, in which it states it has an exclusive right and for which it indicates Canadian and foreign patents have been applied for.

The pictures of the mask which appear in this leaflet are admittedly not that of the defendant corporation but that of the plaintiffs with the label of the defendant corporation stuck over the label of the plaintiffs.

Igor Kaplan, President of the defendant corporation, in an affidavit of the 8th of July, 1968, explained that

Because of the delays of the development work in the LIFE Guard oxygen mask resuscitator, LIFE AID PRODUCTS LIMITED did

> not have its prototype model ready at the time it was intended to release the promotional literature to introduce its LIFE GUARD OXYGEN MASK. As a result one of the units in our possession which I believe, although I cannot positively say, was the unit obtained from H. Simon in England was modified by removing the pull string valve arrangement and by applying the trade mark LIFE GUARD and design label to the cover and by changing the colouring of the device and photographs were taken of this unit and these photographs were used in the illustrations of the device to be marketed by LIFE AID PRODUCTS LIMITED.

The unit which appears, however, in the leaflet, came out in the same colour as plaintiffs' product and the pull string valve which the defendant said it removed, is inside the breathing aperture and cannot be seen.

The above publicity leaflet, therefore, clearly contains a number of untrue and deceptive statements and representations which are calculated to indicate to persons reading the leaflet that the product depicted in the photograph has been manufactured either by or on behalf of the defendant and can be obtained from no one else, when in fact the product produced by the defendant corporation is somewhat different in construction and in colour and the cover is hexagonal instead of being oval shaped.

The statements and representations contained in defendant's publicity leaflets (of which, according to counsel, they still have six thousand) are, therefore, clearly deceptive and although such a course of action may not fall under the prohibition contained in subsections (*a*), (*b*), (*c*) or (*d*) of section 7 of the *Trade Marks Act* it is, in my view, covered by subsection (*e*) thereof in that such statements or representations constitute a deceptive practice as representing to the public as the defendant's device, a device which was produced by somebody else and which also is different from its own device. Such a deliberate and dishonest practice, in addition to being confusing, deceiving and misleading to the public is also contrary to honest commercial usage in this country.

One of the plaintiffs, Therapeutic Research Corporation Limited, the Canadian corporation, is in the process of searching for a Canadian outlet to the devices in which it has obtained the Canadian rights and the above deceptive statements may deter investors and other interested persons who may otherwise be prepared to invest substantial

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sums of money in the purchase of rights for the manufacture, distribution and/or sale of the plaintiffs' product from entering into business relations of any kind with the plaintiffs if the deceptive publicity of the defendant comes to their notice.

I consider that the balance of convenience in the instant case lies with the plaintiffs in that if defendant's circulars are allowed to circulate in the public, they may cause plaintiffs irreparable harm whereas the fact that defendant is restrained from so circulating them may only mean that it is only restricted from advertising its units by means of the objectionable printed circular for a short period of time.

There will therefore be an injunction as sought which, however, will be restricted to restraining the defendant from making any written pictorial or verbal representations or suggestions to the trade or to the public a) that the plaintiffs' devices are manufactured and/or sold by the defendant; b) that any patent rights or rights in any patent application in relation to or in respect of or concerning the oxygen breathing devices of the plaintiffs are owned by or will be owned or obtained by the defendant or any person other than the first plaintiff.[1]

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[1] The pronouncement reads as follows:

Let an injunction go restraining the defendant by itself, its officers, servants or agents, until disposition of this action after trial or other disposition of this action from making any written pictorial or verbal representations or suggestions to the trade or to the public tending to suggest

a) that the oxygen breathing devices manufactured by the third plaintiff are manufactured and/or sold by the defendant;

b) that the oxygen breathing devices imported and/or sold by the first plaintiff are manufactured and/or sold by the defendant;

c) that any patent rights or rights in any patent application in relation to or in respect of or concerning the oxygen breathing devices of the plaintiffs are owned by or will be owned or obtained by the defendant or any person other than the first plaintiff.

Order to contain usual undertaking by the plaintiffs in that the plaintiffs by their counsel undertake to abide by any order which this Court may make as to damages in case this Court should hereafter be of opinion that the defendant should have sustained any by reasons of this order which the plaintiffs ought to pay.

Costs in the cause.

BETWEEN:

FRANK GATTUSO AND MATTEO GATTUSO LIMITED .... PLAINTIFFS;

Montreal 1968

July 3, 4, 9–11

Ottawa July 30

AND

GATTUSO CORPORATION LIMITED ....DEFENDANT.

Trade Marks—Unregistered trade name—Unregistered trade mark—Passing off—Ingredients of—Transfer—Whether effective—Use of registered trade mark by stranger—Whether "distinctive"—Invalidity of registration—Misleading public as to wares—Rights to trade mark arising from use—Power of court—Declaratory judgment—Trade Marks Act, s. 2(f), 7(b), 18(1)(b), 19.

A food products business founded by *P* in 1935 was transferred by him in 1944 to a partnership composed of himself and his two brothers and in 1946 transferred by the partnership to a company they controlled which in 1953 transferred it to defendant, at that time its wholly-owned subsidiary. Certain food products of the business were sold during the years 1935 to 1966 under the trade marks "Savoy" and "Savoia" with labels indicating that the goods were packed by or for "Savoy Products Registered" or "Savoia Products Registered". The first of these trade names was registered by *P* under the Quebec *Partnership Registration Act* in 1940, but no business was carried on under either name. In 1943 *P* became registered owner of the trade mark "Savoy" and transferred that mark to his brother Frank in 1966 after the three brothers had ceased to control defendant. Plaintiff company, which was incorporated at that time, carried on business in the same food products as defendant, using identical labels containing the "Savoy" or "Savoia" trade marks, and Frank sold such goods to the trade as its agent.

Held, an action by Frank and plaintiff company for infringement of the above trade names and trade marks must be dismissed but defendant was entitled to relief against plaintiffs.

1. It was not established (*a*) that Frank carried on business under the trade names or (*b*) that defendant had used the trade names to pass itself off as Frank or its goods as Frank's. (Art. 1835 of the Quebec *Civil Code* respecting the legal consequences of registration of a partnership does not affect the matter).

2. It was not established that *P* retained ownership of the unregistered trade mark "Savoia" after he disposed of his business to the partnership in 1944 (assuming it is possible in law for a person to own an unregistered trade mark when he was not carrying on any business).

3. Assuming that Frank was owner of the registered trade mark "Savoy" its registration was invalid at the time this action was commenced because that mark was then being used by defendant and therefore

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was not "distinctive" within the meaning of s. 2(*f*) of the *Trade Marks Act*: hence its registration was invalid (s. 18(1)(*b*)) and conferred no rights on Frank (s. 19).

4. In directing public attention to plaintiff company's wares in such a way as to cause or be likely to cause confusion in Canada between its wares and those of defendant plaintiff company contravened s. 7(*b*) and defendant was entitled to relief against plaintiffs.

5. Defendant was not entitled to a declaration that it was true owner of the registered trade mark "Savoy" and that the register should be amended accordingly: it did not acquire ownership of the trade mark by transfer from the previous owner and was merely entitled to use the mark by reason of its user of the mark which, the evidence showed, had been abandoned by *P*, its registered owner.

6. The court was not satisfied that it had power to make a declaration that defendant is the sole owner of the unregistered trade mark "Savoia" and the two trade names.

ACTION AND COUNTERCLAIM.

Samuel Wex for plaintiffs.

Samuel Godinsky, Q.C. for defendant.

JACKETT P.:—This is an action and a counterclaim based largely on the same facts. The action is based on a registered trade mark "SAVOY", an unregistered trade mark "SAVOIA", a "trade name 'SAVOY PRODUCTS REGISTERED'" (*registered under the Partnership Declaration Act* of the Province of Quebec), a "trade name 'SAVOIA PRODUCTS REGISTERED'", and a "get-up" or design of a certain label, to all of which the plaintiff Frank Gattuso claims ownership. The second plaintiff, Matteo Gattuso Limited, alleges that it is the exclusive user of the registered trade mark "SAVOY", "the registration whereof is presently pending".

During argument, the claim in respect of the "get-up" or design of a label was abandoned by counsel for the plaintiffs and I need say no more about it. Similarly, during argument, counsel for the plaintiffs abandoned any claim by the corporate plaintiff and the action will therefore be dismissed as against that plaintiff.

The pleadings are prolix and plead so much evidence that it is impossible to establish by reading them what facts are relied on by the parties as being material facts

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that constitute the respective causes of action or substantive defences, and what are pleaded (contrary to the rules of pleading) merely as evidentiary facts that may tend to prove or disprove such material facts. No good purpose would be served by analyzing the pleadings. I shall content myself with revealing as I discuss the matter what, as I understood counsel, are the facts upon which they relied.

Very briefly, the facts may be summarized as follows:

1. The defendant carries on a business of importing, manufacturing, packing and selling certain kinds of foodstuffs, the history of which business is as follows:

(a) One Pasquale Gattuso founded the business as a very young man in 1935;

(b) In 1944 Pasquale Gattuso transferred the business to a partnership consisting of himself and two brothers, Frank Gattuso and Matteo Gattuso, which partnership did business under the name "P. Gattuso Wholesale";

(c) In 1946 the partnership transferred the business to a corporation, Gattuso Olive Oil Corporation (hereinafter referred to as the "Olive Oil Corporation"), in which the three Gattuso brothers thereafter owned all the shares; and

(d) In 1953 the Olive Oil Corporation transferred most of the assets of the business to the defendant company (which the Gattuso brothers had caused to be incorporated to carry on the business and in which the Olive Oil Corporation owned all the shares until 1966), and the defendant has carried on the business since that time.

2. Throughout the period from 1935 to 1966 Pasquale Gattuso, who was president of both of the companies to which I have referred, was the dominating personality in the operation of the business.

3. Throughout that same period also, the goods of the business had been sold under various trade marks of which "GATTUSO" was the one used on most of the

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goods sold and which represented the best class of goods sold. Among the other trade marks used were "SAVOY" and "SAVOIA" (which were, apparently, in the minds of the Gattuso brothers, interchangeable) which were used on cheaper goods that were sold to meet low-priced competition. When the "SAVOY" or "SAVOIA" mark was used, the trade name under which the business was carried on (i.e., Pasquale Gattuso, P. Gattuso Wholesale, Gattuso Olive Oil Corporation, or Gattuso Corporation, Limited) was not shown on the label, which bore, instead, an indication that the goods had been packed by, or for, "SAVOY PRODUCTS REGISTERED" or "SAVOIA PRODUCTS REGISTERED", although, in fact, there was no person carrying on business under either of such appellations during any part of the period 1935 to 1966.

4. In 1966 the Olive Oil Corporation sold a controlling interest in the defendant company to persons not connected with the Gattuso family.

5. The Gattuso brothers ceased to work for the defendant before this action was commenced.

6. In 1940 Pasquale Gattuso filed a declaration under certain provincial legislation that he was carrying on business under the name "SAVOY PRODUCTS REGISTERED". In 1968, after this action was started, he filed a declaration that he had ceased so to carry on business. In fact, he had never carried on business under that name, but his connection with the business in question had been as already indicated, i.e., proprietor until 1944, managing partner until 1946, and president of the operating company until 1966.

7. In 1943 Pasquale Gattuso became registered owner of the trade mark "SAVOY", under the *Unfair Competition Act* and, on November 7, 1966, after the control of the defendant company had been disposed of, he executed a transfer of this registered trade mark to the plaintiff Frank Gattuso, who became the registered owner of the trade mark.

8. After the controlling interest in the defendant company had been disposed of, on August 12, 1966, the plaintiff, Matteo Gattuso Limited, was incorporated and started carrying on business in the same wares as the defendant, using labels to all intents and purposes the same as those described above as having been used by the defendant when utilizing the "SAVOY" or "SAVOIA" trade marks.

The individual plaintiff's case is based on the registered trade mark "SAVOY" and on the contention that Pasquale Gattuso had retained in his personal ownership until 1966 the unregistered trade mark "SAVOIA" and the so-called trade names "SAVOY PRODUCTS REGISTERED" and "SAVOIA PRODUCTS REGISTERED", and that such rights had then somehow been passed to the individual plaintiff.

So far as the so-called trade names are concerned, counsel for the plaintiff has not been able to suggest to me how a person can, apart from statute, have any right in respect of a trade name except where he can show that he was carrying on business under such a name and that some other person has been so using it as to pass himself or his goods or services off for such person or his goods or services. There is no statute relied on here as conferring any special rights on Frank Gattuso in respect of the so-called trade names. There is no suggestion that Frank Gattuso has carried on any business under either of those names. There is no suggestion that any case has been made out that the defendant has, in fact, been passing itself or its wares off as Frank Gattuso or wares manufactured or sold by Frank Gattuso. I reject the claim based on the so-called trade names. I should add that, while it was not suggested that the registration of one of the names in question was under a statute that conferred any special rights on the person on whose behalf it was registered if such person did not carry on business under that name, it was argued that, by virtue of Article 1835 of the Civil Code, that registration operated to make any use of the registered

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name a reference to the person filing the declaration. Article 1835 reads as follows:

> **1835.** The allegations contained in the declaration mentioned in the last preceding article cannot be controverted by any person who has signed the same, nor can they be controverted, as against any party not being a partner, by a person who has not signed but was really a member of the partnership at the time the declaration was made; and no partner, whether he has signed or not, is deemed to have ceased to be a partner until a new declaration has been made and filed aforesaid, stating the alteration in the partnership.

The words particularly relied upon were those after the semicolon: ". . . no partner . . . is deemed to have ceased to be a partner until a new declaration has been made and filed . . ." As I read these words, they can have no application except to a real partnership. I do not understand how they can apply to a person carrying on business alone under a name other than his own. In any event, in the absence of some express statutory provision to the contrary, I take it to be a question of fact as to whether the words "packed" by or for "SAVOY PRODUCTS REGISTERED" or "SAVOIA PRODUCTS REGISTERED", as used through the years by the different proprietors of the business presently carried on by the defendant indicated to the public or the trade that the goods in association with which they were used were made, packed or sold by the proprietor of that business or by Pasquale Gattuso personally, who managed the business for the proprietor and happened to be the person who had filed the declaration under the *Partnership Act* in 1940. The evidence is clear that, in recent years at least, the words in question meant to the trade that the goods were sold by the defendant. There is no evidence that they had any special meaning to any member of the retail purchasing public, but I should be very surprised to learn that any person buying an item of such goods for consumption took the trouble to search the partnership registry. There is certainly no evidence that any member of the public thought that, by reason of the appearance of the words in question, either alone or with one of the trade marks, they were getting wares of Pasquale Gattuso when they were in fact getting wares of the defendant. The plaintiff has not, therefore, any claim for passing off by virtue of these words.[1]

With reference to the unregistered trade mark "SAVOIA", I find the claim that Pasquale Gattuso had retained ownership of it in fact unproven even if it were possible in law for a person to own an unregistered trade mark when he is not carrying on any business. The facts are clear that, under the management of Pasquale Gattuso, this mark was used, after 1944, by the partnership, after 1946 by the Olive Oil Corporation, and for thirteen years after 1953 by the defendant, to distinguish the wares of the person or persons carrying on this business from the wares of others. During that period, Pasquale Gattuso did not carry on business on his own behalf and could not, therefore, have used the trade mark to distinguish goods made or sold by him from those made or sold by others. It follows that, if he did retain it, he must have abandoned it. In fact, it was either passed with the business each time the business changed ownership or, if it did not so pass, with Pasquale Gattuso's full concurrence, it was so used in the business, particularly during the period from 1953 to 1966 when the business was operated by the defendant, that it became a trade mark that distinguished the goods of the person carrying on that business from the goods of others. I find no facts that could give rise to any right in the trade mark belonging to Pasquale Gattuso or to the plaintiff Frank Gattuso.[2]

I turn now to the registered trade mark "SAVOY".

The individual plaintiff's case on the registered trade mark "SAVOY" is that he was, during the relevant period,

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[1] By written notes filed by counsel for the plaintiffs after these reasons were prepared, the claim based on the so-called "trade names" seems to have been dropped, but very much the same argument about the effect of registration of the trade names was put forward as a basis for the claim that Frank Gattuso owned the unregistered trade mark "SAVOIA".

[2] By written notes filed since these reasons were prepared, counsel for the plaintiffs endeavours to support Frank Gattuso's right to the unregistered trade mark "SAVOIA" on the reasoning put forward during argument to support the claim based on the "trade names" that had been "registered". I have already indicated my view of this argument

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the registered owner and had, therefore, by virtue of section 19 of the *Trade Marks Act*, "the exclusive right" to use the mark in Canada in respect of the indicated wares. That section reads as follows:

> **19.** Subject to sections 21, 31 and 65, the registration of a trade mark in respect of any wares or services, unless shown to be invalid, gives to the owner the exclusive right to the use throughout Canada of such trade mark in respect of such wares or services.

(The defendant admits using the trade mark "SAVOY" and that it intends to continue using it. This admission was made by its counsel during argument.) The defendant says that, while the plaintiff was the "registered owner" of the registered trade mark, he was not in fact the "owner" of the mark. Alternatively, the defendant says that, if the plaintiff was the owner of the registered trade mark, the registration is invalid.

As I am satisfied that, if the plaintiff was the "owner" of the registered trade mark, the registration has been "shown", by the evidence adduced by the plaintiff, "to be invalid" (compare section 19), I do not find it necessary, in connection with the main action, to decide whether the plaintiff was the owner of the mark. Either the plaintiff was the owner of the registered trade mark, in which event the registration was invalid and there can be no claim based on the registration under section 19, or the plaintiff was not the owner of the registered mark, in which event the plaintiff can have no cause of action under section 19 based on the registered trade mark. (Any action by the plaintiff on the trade mark "SAVOY" as an unregistered trade mark, apart from the statute, would fail for the reasons that have already been given in connection with the trade mark "SAVOIA".)

I now turn to my reasons for concluding that, on the assumption that the individual plaintiff is the "owner" of the registered trade mark, the registration of the mark is invalid.

Section 18(1)(*b*) says that the registration of a trade mark is invalid if "the trade mark is not distinctive at the time proceedings bringing the validity of the registration into question are commenced". This action brings the validity of the registration of the trade mark "SAVOY" into question and, at the time it was commenced

(a) according to the assumption on which I am discussing the matter, Frank Gattuso was the owner of the mark, and

(b) according to the evidence adduced by the plaintiffs, the mark had been used exclusively in Canada in association with wares of the defendant from 1953 to 1966, since when Matteo Gattuso Limited may also have used the mark in association with its goods.

In these circumstances, I am of opinion that the trade mark was not "distinctive" when this action was commenced, if Frank Gattuso was the owner of the registered trade mark, because section 2(*f*) defines "distinctive" in relation to a trade mark to mean a trade mark that actually distinguishes the wares "in association with which it is used *by its owner*" from "the wares...*of others*". (The italics are mine.) As Frank Gattuso did not, and "others" did, use the registered trade mark in association with goods, in my view, it cannot be said that the mark was "distinctive" within the meaning of the statutory definition when this action was commenced if Frank Gattuso was "its owner". On that assumption, therefore, the registration of the trade mark is invalid by virtue of section 18(1)(*b*) and Frank Gattuso can have no rights under section 19 of the *Trade Marks Act.*

The plaintiffs' action against the defendant will be dismissed for the above reasons.

I turn now to the counterclaim.

As I view the matter, the principal complaint of the defendant against the plaintiffs is that the corporate plaintiff has been directing public attention to its wares in such a way as to cause or be likely to cause confusion in Canada, at the time it commenced so to direct attention to them, between its wares and the wares of the defendant, contrary to section 7(*b*) of the *Trade Marks Act,* and that

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the individual defendant has been a party to such action. I am of opinion, and I so hold, that the evidence adduced by the plaintiffs establishes the soundness of this complaint.

The evidence establishes that Frank Gattuso thought that he had the right to use the two trade marks and the two "trade names" in question, that he purported to authorize the corporate plaintiff to use them, that the corporate plaintiff used labels with such trade marks and "trade names" that were, for all practical purposes, identical with those that the defendant had been using for many years in such manner that they identified its wares to the trade, and that Frank Gattuso, acting as an agent or salesman for the corporate plaintiff, sold goods (and has every intention of continuing to sell goods) with such labels to the trade. By so doing, the corporate plaintiff, acting through the agency of Frank Gattuso, directed attention to its wares in such a way as to cause, or be likely to cause, confusion between its wares and the defendant's wares.[3]

In these circumstances, the Court's power to grant relief is to be found in section 52 of the *Trade Marks Act*, which reads:

> 52. Where it is made to appear to a court of competent jurisdiction that any act has been done contrary to the provisions of this Act, the court may make any such order as the circumstances require including provision for relief by way of injunction and the recovery of damages or profits, and may give directions with respect to the disposition of any offending wares, packages, labels and advertising material and of any dies used in connection therewith.

The trial was conducted on the basis that there should be a reference as to damages or profits if the right thereto should be established. It would seem clear that the defendant should have judgment for damages or profits to be

[3] By written notes filed since these reasons were prepared, counsel for the plaintiffs argues that there can be no claim under section 7(*b*) as long as the registered trade mark is registered in the individual plaintiff's name. This argument seems to be based on a view of section 19 that it confers an exclusive right on the owner of the registered mark *until* the Court delivers a judgment declaring it invalid. It seems clear that this view is fallacious. What section 19 says is that the registration of a trade mark gives the exclusive right of user to the owner "unless shown to be invalid". If the registration is "invalid", it, of course, confers no rights.

ascertained by a reference and for an injunction. This is a case in which there should also be a direction under the concluding words of section 52 designed to ensure that the plaintiff does not continue its offending operations. On a motion for judgment, I shall be glad to hear counsel as to the form that the pronouncement should take.

The defendant also has a claim for a declaration that it is the "sole and true owner" of the unregistered trade mark "SAVOIA" and the so-called trade names. Counsel was, however, unable to refer me to any principle upon which such a declaration might be based.

The defendant claims a declaration that it is the true owner of the registered trade mark "SAVOY" and that the Register should be amended accordingly. This claim raises difficult questions. While I am inclined to the view that a transfer of a registered trade mark may be effective before the transfer is registered,[4] and that a transfer may well be inferred from the facts even though the registered owner has not executed a formal transfer in writing, I am satisfied in this case that Pasquale Gattuso, acting on a misconception of the nature of a trade mark, never did intend to transfer to anybody else, prior to the time he executed the transfer to Frank Gattuso, his registered trade mark "SAVOY". It may well be that, as between Pasquale Gattuso and P. Gattuso Wholesale, there was an implied transfer of the trade mark "SAVOY" in 1944 as part of the goodwill in the business, and that, similarly, as between P. Gattuso Wholesale and the Olive Oil Corporation, there was an implied transfer of the trade mark in 1946 as part of the goodwill of the business, but when, in 1953, the Olive Oil Corporation transferred the assets of the business to the defendant, I cannot find any explicit transfer of the trade mark and I accept the evidence of Pasquale Gattuso that it was not intended to transfer any goodwill or trade mark and, particularly, it was not intended to transfer this mark (which he thought that he owned personally) to the defendant. My view is that, at that time,

[4] See *Wilkinson Sword (Canada) Limited v. Juda* [1968] 2 Ex. C.R. 137.

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the goodwill and the trade marks had been abandoned by all the previous operators of the business when they ceased to operate the business and that the goodwill and the trade marks were then adopted by the defendant and the trade marks were then used to distinguish its goods, and were so used by the defendant that, by the time the corporate plaintiff came into existence, the mark "SAVOY" in fact distinguished the defendant's wares from those of others. My conclusion is, therefore, that the defendant is not the owner of the registration but is entitled to use the trade mark. It did not acquire this right by transfer from a previous owner but by user itself of a mark that, while it had been previously used by someone else, had been abandoned by such person. If the defendant wishes to be registered owner, it will have to apply, as contemplated by the statute, for registration. The claim for a declaration of ownership of the registration is therefore rejected.[5]

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[5] The defendant endeavoured to support its claim to ownership of the registered trade mark on another theory, *viz*,

(a) there were certain assertions that Pasquale Gattuso and Frank Gattuso were operating the business in partnership from a time prior to the registration of the trade mark in Pasquale's name that was evidenced by a certificate issued on July 30, 1943,

(b) a contention that, if the trade mark was being used by such partnership, Pasquale must have registered it as trustee for the partnership, and

(c) a contention that, on each change of ownership of the business, Pasquale, the registered owner, then held the registered trade mark in trust for the new operator of the business, so that, when he transferred it to Frank on November 7, 1966, Frank would hold it as trustee for the defendant.

I reject this contention because

1 on the evidence I hold that the balance of probability is that there was no partnership between Frank and Pasquale prior to 1944 and, as I have already indicated, Pasquale carried on the business during that period on his own behalf;

2 if the mark, at the time of registration, had been adopted by a partnership as contended, rather than by Pasquale personally, Pasquale would not have been entitled to register it (section 22(1) of the *Unfair Competition Act*), and a registration is "invalid" "if the applicant for registration was not the person entitled to secure the registration" (section 18(1) of the *Trade Marks Act*); and

3. having regard to the intrinsic nature of a trade mark, I do not understand how one person can own a trade mark in trust for another, Campare *United States Steel Products Company v. Pittsburg Perfect Fence Co.,* (1917) 19 Ex. C.R. 474.

Finally, as an alternative to its claim that it owns the registered trade mark, the defendant claims a declaration that the registration is invalid. For the reasons already given this claim will be granted.

My conclusions may be summarized as follows:

1. The plaintiff's action is to be dismissed.

2. The defendant will have judgment on the counterclaim against both plaintiffs by reason of "passing off" contrary to section 7(*b*) of the *Trade Marks Act* for

   (a) damages or profits to be determined on a reference,

   (b) an injunction, and

   (c) a suitable direction under the concluding words of section 52 of the *Trade Marks Act.*

3. The defendant will have judgment on the counterclaim based on the finding that the registration of the trade mark "SAVOY" is invalid.

4. Otherwise, the counterclaim will be dismissed.

Upon the application for judgment in accordance with these reasons, in addition to hearing counsel on the form that the pronouncement of judgment should take, I will hear counsel on the question of costs.

Ottawa 1968

May 30–31

Sept. 5

BETWEEN:

GREAT LAKES HOTELS LIMITED ......APPLICANT;

AND

THE NOSHERY LIMITED ....RESPONDENT.

Trade marks—"Penthouse" used in respect of restaurant and catering services and foods in Toronto—Whether "penthouse" descriptive—"Place of origin", meaning—"Distinctive", meaning—Use of trade mark in restricted area—Trade Marks Act, ss. 2(f), 12(1)(b), 18(1)(b).

Respondent, which operated a dining and catering room called "The Penthouse" in its restaurant in Toronto (where it provided both on-premises and off-premises service), became registered owner in 1963 of the word "Penthouse" as a trade mark in respect of its restaurant and catering services and for certain foods. In August 1967 applicant (which operated the "Penthouse Motor Inn" in Toronto) applied under s. 56(1) of the *Trade Marks Act* to strike out the registration.

Held, dismissing the application:—

1. Registration of the word "Penthouse" was not contrary to s. 12(1)(*b*). The word "penthouse", which in modern usage means roof-top-premises, described the location but not the nature or quality of respondent's services or wares. Neither did it describe their place of origin· the words "place of origin" in s. 12(1)(*b*) connote a place indigenous to the services or wares.
2. On the evidence the trade mark "Penthouse" did actually distinguish the services and wares of respondent in metropolitan Toronto at the time these proceedings were commenced and the registration was therefore not invalid under s. 18(1)(*b*). A trade mark is "distinctive" within the meaning of s. 2(*f*) and s. 18(1)(*b*) if it actually distinguishes its owner's services and wares from those of others in a particular restricted area of Canada though not of all others in Canada.

ORIGINATING NOTICE OF MOTION.

James D. Kokonis and *Nicholas H. Fyfe* for applicant.

Gordon F. Henderson, Q.C. and *Kent H. E. Plumley* for respondent.

CATTANACH J.:—These proceedings were initiated by way of an originating notice of motion dated August 30, 1967, pursuant to section 56(1) of the *Trade Marks Act*[1]

[1] 56. (1) The Exchequer Court of Canada has exclusive original jurisdiction, on the application of the Registrar or of any person interested, to order that any entry in the register be struck out or amended on the ground that at the date of such application the entry as it appears on the register does not accurately express or define the existing rights of the person appearing to be the registered owner of the mark.

for an order striking out or amending an entry in the register of trade marks made on February 22, 1963, under No. 130,029 for a trade mark of the word "Penthouse", in the name of the respondent as registered owner, in respect of the following wares and services:

> Services: (1) Restaurant services; catering services (on the premises). (2) Catering services (off the premises); the arrangement, provision and delivery of trays of food for parties commonly referred to as party tray service and buffet tray service.
>
> Wares: Boxed and/or packaged canapes, pates, hors d'œuvres and buffet trays.

On the ground that at the date of the application for registration the entry as it appears on the register does not accurately express or define the existing rights of the registered owner.

The reasons advanced for such allegation by the applicant are set out in its notice of motion as follows:

> (a) The said trade mark was not registrable at the date of registration because at that date it was clearly descriptive or deceptively misdescriptive in the English language of the character or quality of the wares and services for which it is registered and in association with which it is used and of their place of origin;
>
> (b) The said trade mark is not distinctive in that as of the date of institution of these proceedings it does not actually distinguish the wares and services in association with which it is used by the respondent from the wares and services of others, nor is it adapted so to distinguish them.

The date of registration referred to in paragraph (a) above is, of course, February 22, 1963, and date of the commencement of these proceedings referred to in paragraph (b) above is the date of the notice of motion, August 30, 1967.

The applicant, a company incorporated under the laws of the Province of Ontario with head office in Toronto, carries on the business of a motor hotel, including a dining-room and lounge providing entertainment, refreshments and dancing under the name, style or firm of PENTHOUSE MOTOR INN in the municipality of West Hill,

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Scarborough, Ontario. A declaration under the *Partnerships Registration Act*[2] to the effect that the applicant so carried on business since July 29, 1966, was registered on August 3, 1966.

The respondent is also a company incorporated pursuant to the laws of the Province of Ontario. About April 1953 the respondent began the operation of a restaurant known as The Noshery on the ground floor of premises at 488 Eglinton Avenue west, in the City of Toronto, offering on the premises dining facilities.

About May 1958 the respondent began operating a dining and catering room at the same address in association with the name "The Penthouse".

Early in 1961 the respondent began the operation of a catering business whereby it prepared, delivered and served meals, snacks and boxed party trays to individual and to industrial and commercial customers throughout the Municipality of Metropolitan Toronto, which includes Scarborough where the applicant carries on its business, and sometimes beyond the boundaries of that municipal area, under the name of "Penthouse Party Catering".

In December 1963 the respondent opened on its premises a separate room called "The Penthouse Lounge" in which catering to pre-arranged gatherings is carried on.

The respondent's answer to the first of the applicant's objections set forth above is that its trade mark "Penthouse" at the date of its registration, namely, February 22, 1963, was not clearly descriptive or deceptively misdescriptive in the English language of the character or quality of the wares or services in association with which it is used or of their place of origin within the meaning of section 12(1)(*b*) of the *Trade Marks Act.*

The respondent's second answer is that its trade mark of the word "Penthouse" is so adapted to be used by it to distinguish its wares and services from those of others and that as of the date of the institution of these proceedings,

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[2] R S O 1960, 260

namely, August 30, 1967, its trade mark did actually distinguish its wares and services from those of others, (1) throughout Canada, (2) in the Province of Ontario or (3) in the area of Metropolitan Toronto.

The respondent, in its pleadings, also denied that the applicant was a "person interested" and so entitled to apply for an order striking out or amending an entry in the register of trade marks within the meaning of those words in section 56(1) of the *Trade Marks Act*. However, this ground of defence was abandoned at trial.

Counsel for the parties furnished me with a great number of definitions of the word "penthouse" extracted from standard and recognized dictionaries and other sources.

It is apparent therefrom that the word originally referred to, and still refers to, any subsidiary or added structure attached to a larger building and covered by a roof sloping down and away from the main wall of a building. It also describes any bracketed, sloping roof projecting from a wall of a building to give shelter to a door, window or outside stair.

In modern usage the term is applied to any subsidiary roof construction and in particular to structures built above the main roof line and recessed behind the exterior wall line, to house water tanks, elevator machinery (which are now referred to as mechanical penthouses) and, in more recent times, living quarters often of a luxurious nature.

In "A Glossary of House Building Terms" published by Central Mortgage and Housing Corporation, the word, "penthouse" is defined as an enclosed structure, other than a bulk head, on the roof of a building.

With the advent of the plethora of high-rise apartment buildings in urban centres, the landlords have taken liberties with the precise technical meaning of the word "penthouse" and have adopted it to refer to apartments on the topmost floor of the building with the implication that such apartments are more desirable and command a correspondingly higher rental.

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The word "penthouse" is now accepted as referring to premises located upon the roof of a building, or on the topmost floor thereof.

With such background in mind, it is incumbent upon me to determine whether the word "penthouse" is either clearly descriptive or deceptively misdescriptive of the character or quality of the services, as well as the wares, in association with which the respondent has used that trade mark. Those services are, as previously outlined, (1) on the premises restaurant and catering services and (2) off the premises catering services. In these two connections there is no suggestion whatsoever that the trade mark is applicable to the food there supplied, but its use is limited to the services.

The wares in association with which the trade mark "Penthouse" has been used by the respondent are "boxed and/or packaged canapes, pates, hors d'œuvres and buffet trays". The question here is whether or not the word "penthouse" describes their character or quality or their place of origin.

In *Eastman Photographic Materials Company v. Comptroller General of Patents, Designs and Trade Marks*[3], Lord Herschell said at page 580:

> ...any word in the English language may serve as a trade-mark—the commonest word in the language might be employed. In these circumstances it would obviously have been out of the question to permit a person by registering a trade-mark in respect of a particular class of goods to obtain a monopoly of the use of a word having reference to the character or quality of these goods. The vocabulary of the English language is common property: it belongs alike to all; and no one ought to be permitted to prevent the other members of the community from using for purposes of description a word which has reference to the character or quality of goods.
>
> If, then, the use of every word in the language was to be permitted as a trade-mark, it was surely essential to prevent its use as a trade-mark where such use would deprive the rest of the community of the right which they possessed to employ that word for the purpose of describing the character or quality of goods.

Under the *Trade Marks Act* a word in the English language, such as the word "penthouse" may serve as a trade mark subject to the limitations set out in section 12(1)(*b*)

[3] [1898] A.C. 571.

if in the language thereof it is not "either clearly descriptive or deceptively misdescriptive in the English or French languages of the character or quality of the wares or services in association with which it is used or proposed to be used... or of their place of origin;" and if such word is otherwise capable of being used "for the purpose of distinguishing or so as to distinguish wares or services" of the person so using the word from those of others within the meaning of the above quoted words in the definition of a "trade mark" in section 2(*t*) of the Act.

I realize, of course, that the word "Penthouse" describes the location where the on premises catering services supplied by the respondent to the public are performed, but the question is whether or not it describes the services there performed.

To pose the question is to furnish the answer. To describe the location where the services are performed negatives any suggestion that the description is applicable to the on premise services there performed and this would apply with greater force to the off premise services. Neither would the word appear to be clearly descriptive or deceptively misdescriptive of the nature or quality of the wares, as set out above, in association with which the mark is used.

The word "penthouse" is at the utmost suggestive of the character or quality of the services rendered. One might reasonably assume from what I accept as the current usage of the word "penthouse" as referring to premises located on the roof of a building or on the topmost floor thereof that a restaurant so described would be there located. That location, because of its lack of ready access, might well convey an idea of exclusiveness with meals being served where diners could enjoy a leisurely repast with a panoramic view associated with height and consequently an excellent class of food with prices commensurate with the quality of food served in such an exotic and glamorous environment.

However, as I have indicated above, the word "Penthouse" describes the location of the restaurant where such

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services are performed and does not, in my view, refer to the services there performed. Any covert allusion to the character or quality of those services is only remotely suggestive thereof.

This, in my opinion, is not sufficient to render the trade mark not registrable as it has been held in several instances that mere suggestiveness should not deprive a mark of registrability even where a word used skilfully alludes to the wares in association with which it is used unless of course it is clearly descriptive of their character or quality as contemplated by the *Trade Marks Act*. This principle is equally applicable to services.

While I concede that the word "Penthouse" might be remotely suggestive of the character or quality of the services rendered by the respondent in association with its on the premises restaurant and catering services because of the coincidence of the premises and the services, I am unable to follow how such suggestiveness can be present when off the premises catering is performed. These services are described as "the arrangement, provision and delivery of trays of food for parties commonly referred to as party tray service and buffet tray service". I would assume that, in some instances, the only service which the respondent would perform would be to deliver the trays of food ordered by its customer and the actual serving of the food so delivered would be undertaken by the host. I would also assume that, in other instances, the respondent would supply the food and personnel to serve it if desired. In either instance the service so performed would be done at a place far removed from the respondent's on premise service. In either instance there would be no suggestion whatsoever that the service then given would have any relationship to the location of the respondent's on premise services on the roof-top and whatever implications that might be inferred from such circumstance would no longer prevail.

Similarly I am unable to follow how the word "Penthouse" can have any relationship to the respondent's wares in association with which it uses that trade mark. The respondent's wares, to which the trade mark applies, are "boxed and/or packaged canapes, pates, hors d'œuvres

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and buffet trays". The use of the word "Penthouse" in association with such wares does not, in my view, suggest a feature or an essential peculiarity of those wares.

Counsel for the applicant also submitted that the word "Penthouse" is either clearly descriptive or deceptively misdescriptive of the place of origin of the wares and services in association with which it is used. He submitted that the words "place of origin" as they appear in section 12(1)(*b*) must be given a broad meaning, that the word "origin" is synonymous in meaning with words such as "source, inception, beginning, root" and the like, that the word "place" is synonymous in meaning with the word "spot" and accordingly the words "place of origin" must be interpreted as meaning a physical location.

The prohibition in section 12(1)(*b*) is directed against a word that indicates the place of origin of the services or wares. Obviously a word must signify some relationship of the wares to the place to render it not registrable as a trade mark. To be invalid the name must have been given to an article by a trader in such wares to acquire the benefit of a well known and generally recognized connection of the article with the locality. Examples of this readily occur such as "Florida" in association with oranges, "Ceylon, China, or Darjeeling" in association with tea among many others of like import. The name of a place of business or factory, however, is not necessarily descriptive of the place of origin of wares or services unless it can be said that such a name is indigenous to those wares and services.

I fail to follow how the word "penthouse" can have any such connotation. As a matter of first impression the word "Penthouse" does not convey to me any meaning that has a direct relationship with food, catering or restaurant services.

In my view, in any context relating to food the word "Penthouse" in its modern usage appears to be meaningless.

I am, therefore, led to the conclusion that the trade mark "Penthouse", used in association with the wares and

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services above indicated, is not clearly descriptive or deceptively misdescriptive of their character or quality or of their place of origin and from the character of the word it is apparent that it is inherently capable of distinguishing the wares and services of its user.

The applicant's second objection to the registration of the trade mark "Penthouse" by the respondent on February 22, 1963, is that the said trade mark is not distinctive in that at the date of the commencement of these proceedings, i.e. August 30, 1967, it does not actually distinguish the wares and services in association with which it is used by the respondent from the wares and services of others, nor is it adapted to distinguish them.

For the reasons previously outlined I have concluded that the word "penthouse" from its nature is suitable and capable of identifying particular wares and services from those of others.

The question, therefore, remains whether or not it has been established as a fact by the evidence adduced that the trade mark actually in fact distinguishes the wares and services in association with which it is used by the respondent from the wares and services of others.

The word "distinctive" is defined in section 2(*f*) of the *Trade Marks Act* as "in relation to a trade mark means a trade mark that actually distinguishes the wares or services in association with which it is used by its owner from the wares or services of others or is adapted to distinguish them".

Under section 12(2) of the Act a trade mark that is not registrable by reason of it being the name or surname of an individual or clearly descriptive or deceptively misdescriptive of the character or quality of the wares or services or of their place of origin in accordance with paragraphs (*a*) and (*b*) of subsection (1) of section 12 is, nevertheless, registrable if it has been used by the applicant so as to have become distinctive at the date of filing of an application for its registration. The record does not indicate that evidence of distinctiveness was submitted to the Registrar of Trade Marks at that time, i.e. February 28, 1963, but in any event, by reason of section 18(2) no registration of a trade mark that has been so used as to have become distinctive at the date of registration shall be held invalid merely on the ground that evidence of such distinctiveness was not submitted to the Registrar before the grant of registration.

Accordingly, in my view, the critical date to which attention must be directed is that of the commencement of these proceedings, i.e. August 30, 1967, as outlined in section 18(1)(*b*) which reads:

> 18 (1) The registration of a trade mark is invalid if
>
> . . .
>
> (*b*) The trade mark is not distinctive at the time proceedings bringing the validity of the registration into question are commenced;...

The applicant introduced in evidence four affidavits for a two-fold purpose, (1) to establish that the trade mark "Penthouse" was clearly descriptive of the character or quality or the place of origin of the wares and services in association with which it has been used by the respondent and (2) to establish that the mark "Penthouse" is not distinctive because of its multiple use.

With respect to the first purpose, which was to show that the mark is clearly descriptive of the character or quality of the wares and services or of their place of origin, it is my opinion that the affidavits fail to accomplish this end for the reasons I have already given.

It was specifically avowed on behalf of the applicant that these affidavits were not directed to the question of the mark not being registrable because of prior user. Such an allegation is not available to the applicant, whose use of the trade name PENTHOUSE MOTOR INN since July 29, 1966, does not antedate the registration of the trade mark "Penthouse" by the respondent, nor is such allegation raised in the applicant's pleadings.

I have accordingly summarized what I conceive to be the material content of these four affidavits as follows:

1. An affidavit of Harry Lake establishes that he carries on, in the City of Montreal. P.Q. businesses on

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three successive floors of a building owned by him under the respective names of (a) The Elbow Room, (b) The Windsor Steak House and (c) the Penthouse. The Penthouse is operated under a cabaret licence featuring dancing and entertainment. The word Penthouse was registered by him as a firm name and style on January 18, 1951, with the appropriate Provincial authority.

2. An affidavit of Ross Filippone establishes that Eagltime Athletics Ltd. carried on a night club business under the name of The Penthouse in the City of Vancouver, B.C. from March 1947 and continues to do so. This cabaret business includes furnishing restaurant services, dancing, entertainment and music as well as on premises catering by special arrangement. A declaration of the use of the firm name, The Penthouse, was filed on September 1950 with the appropriate Provincial authority.

3. An affidavit of Douglas H. Wymark establishes that Duvernay Enterprises Inc. has operated a night club on the top floor of its premises in the City of Hull, P.Q. under the name of "The Executive Penthouse" since June 1962.

4. An affidavit of Wolfe Margolus establishes that Western Motor Hotel (Edmonton) Ltd. has operated a night club on its premises in the City of Edmonton, Alberta, since May 1963 under the name of Penthouse offering dining, lounge and restaurant services and on premises catering by special arrangement.

The respondent, in its reply, says that the trade mark "Penthouse" did actually distinguish its wares and services from those of others as at August 30, 1967, the date of the commencement of these proceedings, and that it continues to do so (1) in Canada, or (2) in the alternative in the province of Ontario, or (3) in the further alternative in the area of Metropolitan Toronto.

In support of such allegations the respondent introduced in evidence a number of affidavits designed to show that the trade mark "Penthouse" identified its wares and services. These affidavits may be categorized into three groups, (1) those of suppliers to the respondent, (2) those of its competitors and (3) those of the users of its services.

In addition to these affidavits there was also introduced an affidavit of the managing director of the respondent setting out particulars of the respondent's business.

Objections were taken to the probative value of such affidavits and to statements of some of the affiants that in their opinions the trade mark is well known to the public and is distinctive of the wares and services of the respondent. The objection that an affiant cannot express an opinion that a trade mark is distinctive in the public mind is well taken. An affiant can only speak from his own knowledge and cannot express an opinion as to what other persons might think.

In *Battle Pharmaceuticals v. The British Drug Houses Ltd.*,[4] Kerwin J., as he then was, speaking for the Supreme Court of Canada, said at page 53:

> ...We agree that a witness may not state his opinion as to the effect the use of a mark would have, or would be likely to have, . . . because . . . that is the very point to be determined in the proceedings, but that he may testify as to the effect the use of the mark in dispute would have on his own mind.

However, after disregarding the statements which are so inadmissible and giving effect to what I consider to be the probative value of the evidence adduced by the respondent as well as considering the evidence adduced by the applicant I cannot conclude that the respondent's mark distinguishes its wares and services throughout Canada. That claim on the part of the respondent is too ambitious and, in my view, it is not substantiated. From its very nature the business of a restaurant is necessarily local in scope unless a chain of restaurants were operated which is not the case here.

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[4] [1946] S.C.R. 50.

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I am satisfied that the respondent's mark has become well known to the public in the area of the municipality of Metropolitan Toronto. It is apparent from the affidavits filed on behalf of the respondent that it has conducted an extensive on premises and off premises catering service especially from 1962 forward to the present time.

In 1966 and 1967 it served approximately 17,500 meals to customers on its premises in each of those years and in each of those years it also catered to approximately 300 functions on its premises.

Again in those two years it catered to 325 and 328 functions off its premises.

From 1962 it catered to a number of organizations such as service clubs, professional organizations and the like on its own premises and in a location at a shopping centre in the City of Toronto at weekly or monthly luncheon or dinner meetings of those organizations.

On two occasions it catered to large functions at the plant of a leading manufacturer of farm machinery in Brantford, Ontario, and it also conducted a barbecue at an entertainment of a large number of persons by the same manufacturer at its farm at Milliken, Ontario.

It catered to functions in Brampton and New Toronto, Ontario, both of which are in reasonably close proximity to the City of Toronto on one occasion at each of these places and on three occasions to the staff of a resort camp near the Town of Parry Sound, Ontario.

In 1962 it catered to a Bar Mitzvah in North Bay, Ontario, and in 1966 to the silver wedding anniversary of this same customer also held in North Bay.

In my opinion this evidence does not establish that the respondent's mark has become known as identifying its wares and services throughout the Province of Ontario. It does not follow from the fact that on three occasions the respondent catered to functions of the manufacturer mentioned above that the respondent's mark became known to the public generally in Brantford or at Milliken because the parties there were essentially private ones. It only shows that the respondent's services were known to the officials of the manufacturer responsible for arranging the affairs.

The same remarks are applicable to the three functions held near Parry Sound and the two held in North Bay.

I do not consider that this evidence of these isolated and sporadic uses establishes that the respondent's trade mark has become known generally to the public as at August 30, 1967, in those places.

As I have intimated above, I am satisfied from the evidence that the respondent's mark has become well known in the municipality of Metropolitan Toronto. The evidence of two other isolated instances of the respondent catering to functions in Brampton and New Toronto which are in the immediate area of Metropolitan Toronto do not justify me in concluding that the respondent's mark has become known beyond the municipal boundaries of Metropolitan Toronto.

Even if this evidence could be construed as establishing that the respondent's trade mark had become well known in the places mentioned (which I do not think it does) nevertheless it does not identify a geographic area with any degree of precision which would admit of a definition of boundaries.

I am satisfied, on the evidence, that the trade mark "Penthouse" has become "distinctive" in the territorial area of the municipality of Metropolitan Toronto in that it "actually distinguishes the wares or services in association with which it is used" by the respondent in that area as at the date of the institution of these proceedings.

The question then arises whether a mark is "distinctive" within section 18(1)(*b*) as the word "distinctive" is defined in section 2(*f*). It will be recalled that in section 2(*f*) "distinctive" in relation to a trade mark means a trade mark that actually distinguishes the wares or services in association with which it is used by its owner from the wares and services of others. Must that definition of "distinctive" be interpreted as meaning that the trade

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mark must actually distinguish the wares and services of its owner from the wares or services of all others in Canada, or is a trade mark distinctive within the meaning of that definition if it actually distinguishes the wares of its owner from those of others in a very limited area in Canada as, in the present instance, the territorial area of the municipality of Metropolitan Toronto.

I think that a trade mark is distinctive within the meaning of the definition of distinctive in section 2(*f*) if the mark actually distinguishes the wares and services of its owner from the wares or services of others in a particular restricted area of Canada.

In reaching this conclusion I am influenced by section 31(2) of the *Trade Marks Act* which authorizes the Registrar of Trade Marks to restrict the registration of a trade mark to the wares or services in association with which the trade mark is shown, by evidence furnished to the Registrar under subsection (1) of section 32, to have been so used as to have become distinctive and also authorizes the Registrar to restrict the registration to the defined territorial area in Canada in which the trade mark is shown thus to have become distinctive.

It follows irrefutably therefrom that a trade mark is distinctive if it actually distinguishes the wares or services of its owner from those of others in a restricted area of Canada and need not distinguish those wares throughout Canada or from those of all other persons in Canada.

Accordingly the applicant's submission that the trade mark "Penthouse" it not distinctive as at the date of the commencement of those proceedings must fail.

In the result it follows that the applicant's notice of motion is dismissed with costs.

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